



DEPARTMENT OF LABOR

## **Employee Benefits Security Administration**

### **Proposed Exemptions from Certain Prohibited Transaction**

#### **Restrictions**

**AGENCY:** Employee Benefits Security Administration, Labor.

**ACTION:** Notice of proposed exemptions.

**SUMMARY:** This document contains notices of pendency before the Department of Labor (the Department) of proposed exemptions from certain of the prohibited transaction restrictions of the Employee Retirement Income Security Act of 1974 (ERISA or the Act) and/or the Internal Revenue Code of 1986 (the Code). If granted, these proposed exemptions allow designated parties to engage in transactions that would otherwise be prohibited provided the conditions stated there in are met. This notice includes the following proposed exemptions: **Blue Cross and Blue Shield Association, D-12077; Blue Cross and Blue Shield of Kansas City, D-12039; Blue Cross and Blue Shield of Arizona, Inc., D-12035; Blue Cross and Blue Shield of Vermont, D-12055; Hawaii Medical Service Association, D-12038; BCS Financial Corporation, D-12036; Blue Cross and Blue Shield of Mississippi, D-12040; Blue Cross and Blue Shield of Nebraska, Inc., D-12041; BlueCross BlueShield of Tennessee, Inc., D-12045; Triple-S Management Corporation, D-12042; National Account Service Company LLC, D-12049.**

**DATES:** All interested persons are invited to submit written comments or requests for a hearing on the pending exemptions, unless otherwise stated in the Notice of Proposed Exemption, within 45 days from the date of publication of this *Federal Register* Notice.

**ADDRESSES:** All written comments and requests for a hearing should be sent to the Employee Benefits Security Administration (EBSA), Office of Exemption Determinations, U.S. Department of Labor, Attention: Application No. \_\_\_\_\_, stated in each Notice of Proposed Exemption via e-mail to [e-OED@dol.gov](mailto:e-OED@dol.gov) or online through <http://www.regulations.gov> by the end of the scheduled comment period. Any such comments or requests should be sent by the end of the scheduled comment period. The applications for exemption and the comments received will be available for public inspection in the Public Disclosure Room of the Employee Benefits Security Administration, U.S. Department of Labor, Room N-1515, 200 Constitution Avenue, N.W., Washington, D.C. 20210. See SUPPLEMENTARY INFORMATION below for additional information regarding comments.

**SUPPLEMENTARY INFORMATION:**

**Comments:**

In light of the current circumstances surrounding the COVID-19 pandemic caused by the novel coronavirus which may result in disruption to the receipt of comments by U.S. Mail or hand delivery/courier, persons are encouraged to

submit all comments electronically and not to follow with paper copies. Comments should state the nature of the person's interest in the proposed exemption and the manner in which the person would be adversely affected by the exemption, if granted. A request for a hearing can be requested by any interested person who may be adversely affected by an exemption. A request for a hearing must state: (1) The name, address, telephone number, and email address of the person making the request; (2) the nature of the person's interest in the exemption and the manner in which the person would be adversely affected by the exemption; and (3) a statement of the issues to be addressed and a general description of the evidence to be presented at the hearing. The Department will grant a request for a hearing made in accordance with the requirements above where a hearing is necessary to fully explore material factual issues identified by the person requesting the hearing. A notice of such hearing shall be published by the Department in the *Federal Register*. The Department may decline to hold a hearing where: (1) The request for the hearing does not meet the requirements above; (2) the only issues identified for exploration at the hearing are matters of law; or (3) the factual issues identified can be fully explored through the submission of evidence in written (including electronic) form.

**Warning:** All comments received will be included in the

public record without change and may be made available online at <http://www.regulations.gov>, including any personal information provided, unless the comment includes information claimed to be confidential or other information whose disclosure is restricted by statute. If you submit a comment, EBSA recommends that you include your name and other contact information in the body of your comment, but DO NOT submit information that you consider to be confidential, or otherwise protected (such as Social Security number or an unlisted phone number) or confidential business information that you do not want publicly disclosed. However, if EBSA cannot read your comment due to technical difficulties and cannot contact you for clarification, EBSA might not be able to consider your comment. Additionally, the <http://www.regulations.gov> website is an "anonymous access" system, which means EBSA will not know your identity or contact information unless you provide it in the body of your comment. If you send an email directly to EBSA without going through <http://www.regulations.gov>, your email address will be automatically captured and included as part of the comment that is placed in the public record and made available on the Internet.

#### **Notice to Interested Persons**

Notice of the proposed exemptions will be provided to all interested persons in the manner agreed upon by the applicant and the Department, unless otherwise stated in the Notice of Proposed Exemption, within 15 days of the date of publication in the *Federal Register*. Such notice shall include a copy of the notice of proposed exemption as published in the *Federal Register* and shall inform interested persons of their right to comment and to request a hearing (where appropriate).

The proposed exemptions were requested in applications filed pursuant to section 408(a) of the Act and/or section 4975(c)(2) of the Code, and in accordance with procedures set forth in 29 CFR part 2570, subpart B (76 FR 66637, 66644, October 27, 2011).<sup>1</sup> Effective December 31, 1978, section 102 of Reorganization Plan No. 4 of 1978, 5 U.S.C. App. 1 (1996), transferred the authority of the Secretary of the Treasury to issue exemptions of the type requested to the Secretary of Labor. Therefore, these notices of proposed exemption are issued solely by the Department.

The applications contain representations with regard to the proposed exemptions which are summarized below. Interested persons are referred to the applications on file with the Department for a complete statement of the facts and representations.

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<sup>1</sup> The Department has considered exemption applications received prior to December 27, 2011 under the exemption procedures set forth in 29 CFR part 2570, subpart B (55 FR 32836, 32847, August 10, 1990).

**Blue Cross and Blue Shield Association**

**Located in Chicago, Illinois**

**[Application No. D-12077]**

**Proposed Exemption**

The Department is considering granting an exemption under the authority of Section 408(a) of the Employee Retirement Income Security Act of 1974, as amended (ERISA), and Section 4975(c)(2) of the Internal Revenue Code of 1986, as amended (the Code). The proposed exemption relates to legal actions and claims (the Claims) against Allianz Global Investors U.S. LLC (Allianz) and Aon Investments USA Inc. (Aon), that arose from certain losses incurred by the Non-Contributory Retirement Program for Certain Employees of Blue Cross and Blue Shield Association (the Plan) in the first quarter of 2020.<sup>2</sup>

This proposed exemption would permit the Plan sponsor, Blue Cross and Blue Shield Association (BCBSA), to make a series of payments to the Plan, including: (1) the past payment of \$69,000,000, made on March 12, 2021; and (2) the past payment of \$13,500,000, made on March 28, 2022

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<sup>2</sup> In proposing this exemption, the Department is not expressing an opinion regarding the merits of any Claim against Allianz and Aon, or whether the Plan's fiduciaries met their fiduciary duties with respect to Plan assets that are the subject of the Claims. Further, in proposing this exemption, the Department is not limiting any party's claim, demand and/or cause of action arising from the Plan's 2020 first quarter losses in any way. Among other things, this exemption preserves any right, claim, demand and/or cause of action the Plan may have against the following: (1) any fiduciary of the Plan; (2) any fiduciary of the Trust; (3) Blue Cross and Blue Shield Association; and/or (4) any person or entity related to a person or entity described in (1)-(3).

(the Restorative Payments). If the Plan receives litigation proceeds from the Claims, the Plan will transfer the lesser of the litigation proceeds amount or the Restorative Payments amount, plus reasonable attorney fees to BCBSA.

### **SUMMARY OF FACTS AND REPRESENTATIONS<sup>3</sup>**

1. BCBSA is a national association of 35 independent, community-based and locally operated Blue Cross Blue Shield companies. BCBSA owns and manages the Blue Cross and Blue Shield trademarks and names in more than 170 countries around the world and also grants licenses to independent companies to use the trademarks and names in exclusive geographic areas.

2. The Plan is a defined benefit pension plan that covers eligible employees or participants of BCBSA who, as of December 31, 2006, had completed one year of service, reached the age of 21, and remained continuously employed. The Plan was amended effective January 1, 2007 to close participation to new entrants as of December 31, 2006. As

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<sup>3</sup> The Department notes that availability of this exemption is subject to the express condition that the material facts and representations contained in application D-12077 are true and complete at all times and accurately describe all material terms of the transactions covered by the exemption. If there is any material change in a transaction covered by the exemption or in a material fact or representation described in the application, the exemption will cease to apply as of the date of such change. The Summary of Facts and Representations is based on the Applicant's representations, as well as factual representations contained in the Claims' cause of action (as described below) and does not reflect factual findings or opinions of the Department, unless indicated otherwise.

of August 31, 2020, the Plan held \$104,789.042 in total assets.

3. The Plan holds a beneficial interest in the Blue Cross and Blue Shield National Retirement Trust (the Trust). The Trust is a master trust that holds the assets of 16 defined benefit pension plans that participate in the BCBSA's National Retirement Program (the Participating Plans). Northern Trust serves as Trustee and asset custodian to the Trust and maintains separate records that reflect the net asset value of each Participating Plan. The Trust's earnings, market adjustments, and administrative expenses are allocated among the Participating Plans based on the respective Participating Plan's share of the Trust's assets. A Participating Plan's interest in the Trust's net assets is based on its share of the Trust.

4. The Committee serves as named fiduciary and administrator for each Participating Plan. The Committee is a standing committee of the BCBSA's board of directors. In 2011, the Committee invested a portion of the Trust's assets in funds managed by Allianz Global Investors U.S. LLC (Allianz), as part of a Structured Alpha Investment Strategy. These funds included: (a) AllianzGI Structured Alpha Multi-Beta Series LLC I; (b) AllianzGI Structured Alpha Emerging Markets Equity 350 LLC; and (c) AllianzGI



Structured Alpha 1000 LLC (collectively, the Structured Alpha Funds).

5. The Applicant represents that the Allianz Structured Alpha strategy consisted of alpha and beta components. According to the Applicant, the alpha component was an options trading strategy that Allianz claimed would seek targeted positive return potential while maintaining structural risk protections. The beta component was intended to provide broad market exposure to a particular asset class through investments in financial products similar to an exchange-traded fund that replicates the performance of a market index, such as the S&P 500. According to the Applicant, Allianz represented that the Structured Alpha Strategy would capitalize on the return-generating features of option selling (short volatility) while simultaneously benefitting from the risk-control attributes associated with option buying (long volatility). According to the Applicant, Allianz represented further that the alpha component would include position hedging consisting of long-volatility positions designed to protect the portfolio in the event of a market crash.

6. As of December 31, 2019, the total market value of the Plan's portion of the Trust's investment in the Allianz

Structured Alpha Funds was \$224,525,108. At the time, this represented 77.66% of total Plan assets.<sup>4</sup>

7. In 2009, the Committee retained Aon (then called Ennis Knupp) to provide investment advice regarding the investment of Plan assets held in the Trust. The Applicant represents that Aon provided regular investment advice pursuant to a written contract between it and the Committee. Pursuant to its engagement, Aon agreed to provide the following: "recommendations to [the Committee] regarding asset allocation" within the Trust; "recommendations to [the Committee] regarding the specific asset allocation and other investment guidelines" for the Trust's investment managers such as Allianz; and advice "regarding the diversification of assets" held in the Trust." The Applicant represents that Aon agreed to: conduct "active, ongoing monitoring" of Allianz to "identify any forward-looking" risks "that could impact performance;" and "inform itself" of any information necessary to discharge its duty to monitor, including information about the actual options positions Allianz had constructed.

8. The Applicant represents that when equity markets sharply declined in February and March of 2020, volatility spiked and the options positions held within the Structured

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<sup>4</sup> By proposing this exemption, the Department does not, in any way, suggest a conclusion that the Plan's fiduciaries met their ERISA Section 404 duties when they caused the Trust to invest 77.66% of the Plan's total assets in the Allianz Structured Alpha Funds.

Alpha Strategy were exposed to a heightened risk of loss. The Applicant represents that, unbeknownst to the Committee, and in violation of Allianz's stated investment strategy, Allianz abandoned the hedging strategy that was the supposed cornerstone of the Structured Alpha Strategy, leaving the portfolio almost entirely unhedged against a spike in market volatility. As described in the Claims, although Allianz had represented that it would buy hedges at strike prices ranging from 10% to 25% below the market, the hedges it actually held at the end of February 2020 were as much as 60% below the market.

The Applicant represents that, as of January 31, 2020, the Trust had invested approximately \$2,916,049,486 in the Structured Alpha Strategy. Six weeks later, the Trust faced a margin call, which the Applicant states left it no choice but to liquidate the investment. The Trust was ultimately able to redeem only \$646,762,678 of its \$2,916,049,486 investment, resulting in a total loss of \$2,269,286,808.

Specifically, regarding the Plan's portion of the loss, as of December 31, 2019, the market value for the Plan's assets totaled \$289,100,229. As of March 31, 2020, the market value of total assets for the Plan decreased to \$97,181,664. The Applicant represents that the Plan's total losses from the Allianz Structured Alpha Strategy was \$183,368,144, which caused the Plan to be underfunded.

9. On September 16, 2020, the Committee filed a cause of action in the United States District Court for the Southern District of New York (Case number 20-CIV-07606) against Allianz and Aon for Breach of Fiduciary Duty under ERISA Section 404, Breach of Co-Fiduciary Duty under ERISA Section 405, and violation of ERISA Section 406(b) for managing the Plan assets in its self-interest and breach of contract. It is possible that resolution of this claim and other legal actions against Allianz and Aon in connection with the Plan's losses (the Claims) could take an extended period of time.

10. The Applicant states that rather than wait for the Claims to be resolved, BCBSA took steps to protect Plan benefits and avoid onerous benefit restrictions under Code section 436 that could apply to the Plan as a result of a funding shortfall. Therefore, on November 24, 2020, BCBSA and the Plan entered into a Contribution and Assignment Agreement (the Contribution and Assignment Agreement).

11. Pursuant to the Contribution and Assignment Agreement, BCBSA agreed to make the Restorative Payments to the Plan consisting of: (a) a payment not to exceed \$74,000,000 by September 30, 2021; (b) a payment not to exceed \$20,000,000 by September 30, 2022; and (c) a payment not to exceed \$31,000,000 by September 30, 2023. Thereafter, BCBSA made Restorative Payments to the Plan of

\$69,000,000 on March 12, 2021, and \$13,500,000 on March 28, 2022.

12. On June 22, 2022, BCBSA and the Plan amended the Restorative Payments provision of the Contribution and Assignment Agreement to provide that BCBSA's Restorative Payments under the Agreement will consist only of the \$69,000,000 payment made on March 12, 2021, and the \$13,500,000 payment made on March 28, 2022.

13. In exchange for the Restorative Payments, the Plan assigned to BCBSA its right to retain certain litigation and/or settlement proceeds recovered from the Claims (the Assigned Interests).<sup>5</sup> Per the assignment, once the Allianz/Aon litigation is resolved and if the Plan receives litigation proceeds from the Claims, the Plan will transfer to BCBSA a repayment (the Repayment) that does not exceed the total Restorative Payments made by BCBSA, plus reasonable attorney fees paid by BCBSA on behalf of the Plan in connection with the Claims, if such fees are reviewed and approved by a qualified independent fiduciary who confirms that the fees were reasonably incurred and paid by BCBSA to unrelated third parties (the Attorney Fees). For the purposes of this exemption, Attorney Fees reimbursable to BCBSA do not include: (a) legal expenses

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<sup>5</sup> Under the Contribution and Assignment Agreement, if the Plan receives litigation or settlement proceeds from the Claims, the proceeds would first flow to the Trust, and then each Plan's pro rata portion of the proceeds would be deposited into the individual trust funding that Plan.

paid by the Plan; and (b) legal expenses paid by BCBSA for representation of its own interests or the interests of any party other than the Plan. For purposes of determining the amount of Attorney Fees the Plan may reimburse to BCBSA under this exemption, the amount of reasonable attorney fees paid by BCBSA on behalf of the Plan in connection with the Claims must be reduced by the amount of legal fees received by BCBSA in connection with the Claims from any non-Plan party (for example, from a third party pursuant to a court award).

14. The Plan must ultimately receive at least the full value of the promised Restorative Payments (\$82,500,000), minus the Attorney Fees. The Plan may ultimately receive more than the Restorative Payment amount required under the Contribution and Assignment Agreement. If the Plan receives litigation or settlement proceeds that exceed the amount of Restorative Payments that BCBSA has made to the Plan, the Plan's Repayment to BCBSA will be limited to the amount of Restorative Payments actually made by BCBSA, plus Attorney Fees. For example, if BCBSA reasonably incurred \$100,000 in Attorney Fees and the Plan receives \$120,000,000 in litigation proceeds, the Plan will make a Repayment to BCBSA totaling \$82,600,000.

15. Alternatively, if the Plan receives less litigation or settlement proceeds than the amount of Restorative Payments that BCBSA has made to the Plan, the

Plan will transfer to BCBSA the lesser amount of litigation or settlement proceeds, plus Attorney Fees. For example, if BCBSA has reasonably incurred \$100,000 in Attorney Fees and the Plan receives \$50,000,000 in litigation proceeds, the Plan will make a Repayment to BCBSA totaling \$50,100,000.

16. The Department notes that if the Plan receives any restitution that is tied to the conduct underlying the Claims but was ordered pursuant to a proceeding or directive that is external to Case number 20-CIV-07606, the disposition of such proceeds must conform to the requirements of this exemption.

17. BCBSA retained Gallagher Fiduciary Advisors, LLC (Gallagher or the Independent Fiduciary) of New York, New York, to serve as the Plan's independent fiduciary with respect to the Required Restorative Payments and the potential repayment by the Plan of those Payments (collectively, the Proposed Transactions). Gallagher represents that it has extensive experience in institutional investment consulting and fiduciary decision-making regarding traditional and alternative investments. Gallagher further represents that its independent fiduciary decision-making work involves acting as a fiduciary advisor or decision-maker for plans and other ERISA-regulated asset pools and that it has experience with a wide range of asset classes and litigation claims.

18. Gallagher represents that it understands its duties and responsibilities under ERISA in acting as a fiduciary on behalf of the Plan. Gallagher also acknowledges that it is authorized to take all appropriate actions to safeguard the Plan's interests, and that it will monitor the Proposed Transactions on the Plan's behalf on a continuous basis and throughout the term required by this exemption.

19. Gallagher represents that it does not have any prior relationship with any parties in interest to the Plan, including BCBSA and any BCBSA affiliates. Gallagher further represents the total revenues it has received from the Plan and from parties in interest to the Plan in connection with its engagement as Independent Fiduciary represents approximately 0.78% of Gallagher's total revenue.

20. Gallagher represents that no party associated with this exemption application has or will indemnify it, in whole or in part, for negligence of any kind and/or any violation of state or federal law that may be attributable to Gallagher's performance of its duties as Independent Fiduciary to the Plan with respect to the Proposed Transactions. In addition, no contract or instrument entered into by Gallagher as Independent Fiduciary may purport to waive any liability under state or federal law for any such violation.



21. On November 23, 2020, Gallagher completed an Independent Fiduciary Report (the Independent Fiduciary Report) finding that the massive losses caused by the Trust's investment in the Allianz Structured Alpha Strategy resulted in a significant reduction to the Plan's total assets and funding level. Gallagher represents that the Required Restorative Payments, which will be received by the Plan substantially in advance of a final resolution of the Claims against Allianz and Aon, should restore the Plan's funded percentage to its pre-loss funded percentage as of January 1, 2019. The restoration of the Plan's funding status will secure ongoing benefit payments to participants and beneficiaries.

Gallagher notes that the Contribution and Assignment Agreement provides that the Trust must reimburse BCBSA only up to the Required Restorative Payment Amount already received, plus any reasonable legal expense paid to non-BCBSA-related parties that were incurred by, or allocated to, BCBSA as a result of the Claims.<sup>6</sup> Thus, if the Plan's ultimate recovery amount from the Claims is less than the Required Restorative Payment Amount, plus related

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<sup>6</sup> Currently, legal fees and expenses associated with the Claims are being paid by most of the Participating Plan's trusts on a pro rata basis according to each Participating Plan's total invested assets held in the Master Trust's Allianz Structured Alpha Strategy before the losses were incurred in the first quarter 2020. The Applicant represents that the Committee reviews and approves these legal fees before passing them through to each Participating Plan.

litigation expenses that were allocated to the Plan, BCBSA, not the Plan, will suffer the loss.

Gallagher states that the Proposed Transactions and the terms of the Contribution and Assignment Agreement were negotiated and approved by Gallagher in its role as the Plan's Independent Fiduciary. Gallagher states that it approved the Proposed Transactions only after conducting an extensive analysis of the damages suffered by the Plan as a result of the failed Allianz Structured Alpha Strategy. Gallagher represents that it conducted numerous discussions with Trust representatives and counsel, along with the Plan's representatives and counsel to ensure that the interests of the Plan's participants and beneficiaries were protected with respect to all aspects of the Proposed Transactions. Based upon its assessment, Gallagher approved the Plan's receipt of the Required Restorative Payments from BCBSA in exchange for the Assignment.

#### ERISA Analysis

22. Absent an exemption, the Plan's receipt of the Restorative Payments from BCBSA in exchange for the Plan's transfer of litigation or settlement proceeds to BCBSA would violate ERISA. In this regard, ERISA Section 406(a)(1)(A) prohibits a plan fiduciary from causing the plan to engage in a transaction if the fiduciary knows or should know that such transaction constitutes a direct or indirect sale or exchange of any property between a plan

and a party in interest. BCBSA, as an employer whose employees are covered by the Plan, is a party in interest with respect to the Plan under ERISA Section 3(14)(C). The Required Restorative Payments to the Plan and the Plan's potential repayment to BCBSA with litigation or settlement proceeds would constitute impermissible exchanges between the Plan and a party-in-interest (BCBSA) in violation of ERISA Section 406(a)(1)(A).

ERISA Section 406(a)(1)(D) prohibits a plan fiduciary from causing a plan to engage in a transaction if the fiduciary knows or should know that the transaction constitutes a direct or indirect transfer to, or use by or for the benefit of, a party-in-interest, of the income or assets of the plan. The transfer of Plan assets to BCBSA in connection with the Repayment would constitute an impermissible transfer of Plan assets to a party-in-interest in violation of ERISA Section 406(a)(1)(D).

#### Conditions

23. This proposed exemption contains a number of conditions that must be met. For example, the proposed exemption mandates that the Independent Fiduciary, in full accordance with its obligations of prudence and loyalty under ERISA Section 404(a)(1)(A) and (B) must:

(a) review, negotiate, and approve the terms and conditions of the Required Restorative Payments, the Repayment, and the Contribution and Assignment Agreement,

before the Plan enters into such payments and the agreement;

(b) determine that the terms and conditions of the Required Restorative Payments, the Repayment, and the Contribution and Assignment Agreement are prudent, in the interest of the Plan and its participants and beneficiaries, and protective of the rights of the Plan's participants and beneficiaries;

(c) confirm that the Required Restorative Payments are fully and timely made;

(d) monitor the Claims and confirm that the Plan receives its proper share of any litigation or settlement proceeds received by the Trust in connection with the Claims;

(e) ensure that any Repayment by the Plan to BCBSA fully complies with the terms of this exemption and is for no more than the lesser of the total Restorative Payments actually made to the Plan by BCBSA or the amount the Plan received from the Claims, plus Attorney Fees;

(f) ensure that any Repayment by the Plan to BCBSA for legal expenses in connection with the Claims is limited to only reasonable legal expenses that were paid by BCBSA to unrelated third parties for representation of the Plan and its interests (as opposed to representation of BCBSA or the interests of any party other than the Plan) where BCBSA was not otherwise reimbursed from a non-Plan party;

(g) monitor the Plan's Assigned Interests on an ongoing basis to determine and confirm that any excess recovery amount from the Claims (i.e., any amount that exceeds the Required Restorative Payment Amount) is retained by the Plan;

(h) ensure that all of the conditions and definitions of this proposed exemption are met; and

(i) represent that it has not and will not enter into any agreement or instrument that violates ERISA Section 410 or Department Regulations codified at 29 CFR section 2509.75-4.<sup>7</sup>

24. This proposed exemption also requires Gallagher to respond in writing to any information requests from the Department regarding Gallagher's activities as the Plan's Independent Fiduciary. Additionally, no later than 90 days after the resolution of the litigation, Gallagher must submit a written report to the Department demonstrating that all terms and conditions of the exemption have been met.

25. This proposed exemption requires that the Plan has not and will not release any claims, demands and/or causes of action it may have against: (a) any fiduciary of the Plan; (b) any fiduciary of the Trust; (c) BCBSA; and/or

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<sup>7</sup> ERISA Section 410 provides, in part, that "except as provided in ERISA Sections 405(b)(1) and 405(d), any provision in an agreement or instrument which purports to relieve a fiduciary from responsibility or liability for any responsibility, obligation, or duty under this part [meaning Part 4 of Title I of ERISA] shall be void as against public policy."

(d) any person or entity related to a person or entity described in (a)-(c) of this paragraph. Additionally, any Repayment by the Plan to BCBSA must be made in a manner designed to minimize unnecessary costs and disruption to the Plan and its investments.

26. The Plan may not make any Repayment to BCBSA before the date: the Plan has received from BCBSA the entire amount of the Restorative Payments agreed to in the Amended Contribution and Assignment Agreement; and all the Claims are settled. Furthermore, the Plan may not pay any interest to BCBSA in connection with its receipt of the Required Restorative Payments, nor pledge Plan assets to secure any portion of the Required Restorative Payments.

27. Pursuant to this proposed exemption, the Plan may not incur any expenses, commissions or transaction costs in connection with the Proposed Transactions. However, as noted above, under certain circumstances the Plan may reimburse BCBSA for reasonable legal expenses arising from the Claims that BCBSA paid to non-BCBSA-related parties for representation of the Plan and its interests (as opposed to representation of BCBSA or the interests of any party other than the Plan) where BCBSA was not otherwise reimbursed by a non-Plan party.

28. Finally, the exemptive relief provided under this proposed exemption is conditioned upon the Department's assumption that the material facts and representations set

forth above in the Summary of Facts and Representation section are true and accurate at all times. In the event that a material fact or representation detailed above is untrue or inaccurate, the exemptive relief provided under this exemption will cease immediately.

### Statutory Findings

29. ERISA Section 408(a) provides, in part, that the Department may not grant an exemption unless the Department finds that the exemption is administratively feasible, in the interest of affected plans and of their participants and beneficiaries, and protective of the rights of such participants and beneficiaries. Each of these criteria is discussed below.

a. The Proposed Exemption Is "Administratively Feasible." The Department has tentatively determined that the proposed exemption is administratively feasible because, among other things, the Independent Fiduciary will represent the interests of the Plan for all purposes with respect to the Proposed Transactions.<sup>8</sup> In this regard, not later than 90 days after the resolution of the litigation, the Independent Fiduciary must submit a written report to the

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<sup>8</sup> This proposed exemption would require that if the Independent Fiduciary resigns, is removed, or for any reason is unable to serve as an Independent Fiduciary, the successor Independent Fiduciary must, among other things, assume all of the duties of the outgoing Independent Fiduciary. As soon as possible, including before the appointment of a successor Independent Fiduciary, the Plan Sponsor and the Plan must notify the Department's Office of Exemption Determinations of the change in Independent Fiduciaries. The notification must contain all material information including the qualifications of the successor Independent Fiduciary.

Department demonstrating that all of the requirements of this exemption have been met.

b. The Proposed Exemption Is "In the Interests of the Plan." The Department has tentatively determined that the proposed exemption is in the interest of the Plan because, among other things, the Plan's receipt of the Required Restorative Payments substantially improved the Plan's funding status, which enhanced the Plan's ability to meet its obligations to fund benefit obligations to participants and beneficiaries and helped the Plan avoid the imposition of benefit limitations imposed under Code section 436.

c. The Proposed Exemption Is "Protective of the Plan." The Department has tentatively determined that the proposed exemption is protective of the rights of the Plan's participants and beneficiaries because, among other things, the Plan will repay BCBSA the lesser of the Required Restorative Payment Amount, or the amount the Plan receives in proceeds from the Claims, ensuring that the Proposed Transactions will result in an increase in Plan assets of at least the total amount of Restorative Payments (less reasonable legal expenses related to the Claims paid by BCBSA to unrelated third parties, as confirmed and approved by the Independent Fiduciary). Further, this exemption preserves any right, claim, demand and/or cause of action the Plan may have against: (a) any fiduciary of the Plan; (b) any fiduciary of the Trust; (c) BCBSA; and/or (d) any



person or entity related to a person or entity described in (a) - (c).

### Summary

30. Based on the conditions described above, the Department has tentatively determined that the relief sought by the Applicant satisfies the statutory requirements under ERISA Section 408(a) for the Department to make findings that support its issuance of a proposed exemption.

### **PROPOSED EXEMPTION**

The Department is considering granting an exemption under the authority of ERISA Section 408(a) and Code Section 4975(c)(2) and in accordance with the procedures set forth in the Department's exemption procedure regulation.<sup>9</sup>

### **Section I. Definitions**

(a) The term "Attorney Fees" means reasonable legal expenses paid by BCBSA on behalf of the Plan in connection with the Claims, if such fees are reviewed and approved by a qualified independent fiduciary who confirms that the fees were reasonably incurred and paid by BCBSA to unrelated third parties. For the purposes of this exemption, the Attorney Fees reimbursable to BCBSA do not

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<sup>9</sup> 29 CFR part 2570, subpart B (55 FR 32836, 32847, August 10, 1990).

include: (1) legal expenses paid by the Plan; and (2) legal expenses paid by BCBSA for representation of BCBSA or the interests of any party other than the Plan.

(b) The term "BCBSA" means Blue Cross and Blue Shield Association.

(c) The term "Claims" means the legal claims against Allianz Global Investors U.S. LLC (Allianz) and Aon Investments USA Inc. (Aon), to recover certain losses incurred by the Plan in the first quarter of 2020.

(d) The term "Contribution and Assignment Agreement" means the written agreement dated November 24, 2020, and its amendment that became effective on June 22, 2022, containing all material terms regarding BCBSA's agreement to make Required Restorative Payments to the Plan in return for the Plan's potential Repayment to BCBSA of an amount that is no more than lesser of the Required Restorative Payment Amount (as described in Section I(h)) or the amount of litigation proceeds the Plan receives from the Claims, plus reasonable attorney fees paid to unrelated third parties by BCBSA in connection with the Claims.

(e) The term "Independent Fiduciary" means Gallagher Fiduciary Advisors, LLC (Gallagher) or a successor Independent Fiduciary to the extent Gallagher or the successor Independent Fiduciary continues to serve in such capacity who:

(1) Is not an affiliate of BCBSA and does not hold an ownership interest in BCBSA or affiliates of BCBSA;

(2) Was not a fiduciary with respect to the Plan before its appointment to serve as the Independent Fiduciary;

(3) Has acknowledged in writing that it:

(i) is a fiduciary with respect to the Plan and has agreed not to participate in any decision regarding any transaction in which it has an interest that might affect its best judgment as a fiduciary; and

(ii) Has appropriate technical training or experience to perform the services contemplated by the exemption;

(4) Has not entered into any agreement or instrument that violates the prohibitions on exculpatory provisions in ERISA Section 410 or the Department's regulation relating to indemnification of fiduciaries;<sup>10</sup>

(5) Has not received gross income from BCBSA or its affiliates during any fiscal year in an amount that exceeds two percent (2%) of the Independent Fiduciary's gross income from all sources for the prior fiscal year. This provision also applies to a partnership or corporation of which the Independent Fiduciary is an officer, director, or 10 percent (10%) or more partner or shareholder, and includes as gross income amounts received as compensation

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<sup>10</sup> 29 CFR 2509.75-4.

for services provided as an independent fiduciary under any prohibited transaction exemption granted by the Department; and

(6) No organization or individual that is an Independent Fiduciary, and no partnership or corporation of which such organization or individual is an officer, director, or ten percent (10%) or more partner or shareholder, may acquire any property from, sell any property to, or borrow any funds from BCBSA or from affiliates of BCBSA while serving as an Independent Fiduciary. This prohibition will continue for six months after the party ceases to be an Independent Fiduciary and/or the Independent Fiduciary negotiates any transaction on behalf of the Plan during the period that the organization or individual serves as an Independent Fiduciary.

(f) The "Plan" means the Non-Contributory Retirement Program for Certain Employees of Blue Cross and Blue Shield Association.

(g) The term "Plan Losses" means the \$183,368,144 in Plan losses the BCBSA's National Employee Benefits Committee alleges were the result of breaches of fiduciary responsibilities and breaches of contract by Allianz Global Investors U.S. LLC and/or Aon Investments USA Inc.

(h) The term "Restorative Payments" means the payments made by BCBSA to the Plan in connection with the Plan

Losses, defined above, consisting of: (1) the past payment of \$69,000,000 on March 12, 2021; and (2) the past payment of \$13,500,000 on March 28, 2022. The sum of (1)-(2) is the Required Restorative Payment Amount.

(i) The "Repayment" means the payment, if any, that the Plan will transfer to BCBSA following the Plan's receipt of proceeds from the Claims, where the Repayment is made following the full and complete resolution of the Claims; and in a manner that is consistent with the terms of the exemption.

## **Section II. Proposed Transactions**

If the proposed exemption is granted, the restrictions of ERISA Sections 406(a)(1)(A), (B) and (D) and the sanctions resulting from the application of Code Section 4975, by reason of Code Sections 4975(c)(1)(A), (B) and (D), shall not apply, effective November 24, 2020, to the following transactions: BCBSA's transfer of Restorative Payments to the Plan; and, in return, the Plan's Repayment of an amount to BCBSA, which must be no more than the lesser of the Restorative Payment Amount or the amount of litigation proceeds the Plan received from the Claims, plus reasonable Attorney Fees, provided that the Definitions set forth in Section I and the Conditions set forth in Section III are met.

## **Section III. Conditions**

(a) The Plan received the entire Restorative Payment Amount no later than March 28, 2022;

(b) In connection with its receipt of the Required Restorative Payments, the Plan does not release any claims, demands and/or causes of action the Plan may have against the following: (1) any fiduciary of the Plan; (2) any fiduciary of the Trust; (3) BCBSA; and/or (4) any person or entity related to a person or entity identified in (1)-(3) of this paragraph;

(c) The Plan's Repayment to BCBSA is for no more than the lesser of the total Restorative Payments received by the Plan or the amount of litigation proceeds the Plan receives from the Claims. The Plan's Repayment to BCBSA may only occur after the Independent Fiduciary has determined that: all the conditions of the exemption are met; the Plan has received all the Restorative Payments it is due; and the Plan has received all the litigation proceeds it is due. The Plan's Repayment to BCBSA must be carried out in a manner designed to minimize unnecessary costs and disruption to the Plan and its investments;

(d) A qualified independent fiduciary (the Independent Fiduciary, as further defined in Section II(e)), acting solely on behalf of the Plan in full accordance with its obligations of prudence and loyalty under ERISA Sections 404(a)(1)(A) and (B) must:

(1) Review, negotiate and approve the terms and

conditions of the Restorative Payments and the Repayment and the Contribution and Assignment Agreement, all of which must be in writing, before the Plan enters into those transactions/agreement;

(2) Determine that the Restorative Payments, the Repayment, and the terms of the Contribution and Assignment Agreement, are prudent and in the interest of the Plan and its participants and beneficiaries;

(3) Confirm that the Required Restorative Payment Amount was fully and timely made;

(4) Monitor the litigation related to the Claims and confirm that the Plan receives, in a timely manner, its proper share of any litigation or settlement proceeds received by the Trust;

(5) Ensure that any Repayment by the Plan to BCBSA for legal expenses in connection with the Claims is limited to only reasonable legal expenses that were paid by BCBSA to unrelated third parties;

(6) Ensure that all of the conditions and definitions of this proposed exemption are met;

(7) Submit a written report to the Department's Office of Exemption Determinations demonstrating and confirming that the terms and conditions of the exemption were met, within 90 days after the Repayment; and

(8) Not enter into any agreement or instrument that violates ERISA Section 410 or the Department's Regulations codified at 29 CFR Section 2509.75-4.

(f) The Plan pays no interest in connection with the Restorative Payments;

(g) The Plan does not pledge any Plan assets to secure any portion of the Restorative Payments;

(h) The Plan does not incur any expenses, commissions, or transaction costs in connection with the Proposed Transactions. However, if first approved by the Independent Fiduciary, the Plan may reimburse BCBSA for reasonable legal expenses paid in connection with the Claims by BCBSA to non-BCBSA-related parties. For purposes of determining the amount of Attorney Fees the Plan may reimburse to BCBSA under this proposal, the amount of reasonable attorney fees paid by BCBSA on behalf of the Plan in connection with the Claims must be reduced by the amount of legal fees received by BCBSA in connection with the Claims from any non-Plan party (i.e., pursuant to a court award);

(i) The proposed transactions do not involve any risk of loss to either the Plan or the Plan's participants and beneficiaries;

(j) No party associated with this exemption has or will indemnify the Independent Fiduciary and the Independent Fiduciary will not request indemnification from



any party, in whole or in part, for negligence and/or any violation of state or federal law that may be attributable to the Independent Fiduciary in performing its duties to the Plan with respect to the Proposed Transactions. In addition, no contract or instrument may purport to waive any liability under state or federal law for any such violation.

(k) If an Independent Fiduciary resigns, is removed, or for any reason is unable to serve as an Independent Fiduciary, the Independent Fiduciary must be replaced by a successor entity that: (1) meets the definition of Independent Fiduciary detailed above in Section II(e); and (2) otherwise meets all of the qualification, independence, prudence and diligence requirements set forth in this exemption. Further, any such successor Independent Fiduciary must assume all of the duties of the outgoing Independent Fiduciary. As soon as possible, including before the appointment of a successor Independent Fiduciary, BCBSA must notify the Department's Office of Exemption Determinations of the change in Independent Fiduciary and such notification must contain all material information regarding the successor Independent Fiduciary, including the successor Independent Fiduciary's qualifications; and

(1) All of the material facts and representations set forth in the Summary of Facts and Representation are true and accurate at all times.

#### NOTICE TO INTERESTED PERSONS

The Applicant will give notice of the proposed exemption to all interested persons and all of the parties to the litigation described above, within fifteen calendar days after the publication of the notice of proposed exemption in the *Federal Register*. The notice will contain a copy of the notice of proposed exemption, as published in the *Federal Register*, and a supplemental statement, as required pursuant to the Department's regulations codified at 29 CFR 2570.43(a)(2). The supplemental statement will inform interested persons of their right to comment on the pending exemption. Written comments are due by **[INSERT DATE THAT IS 45 DAYS FROM THE PUBLICATION OF THE NOTICE IN THE *FEDERAL REGISTER*]**.

All comments will be made available to the public.

**Warning:** If you submit a comment, EBSA recommends that you include your name and other contact information in the body of your comment, but DO NOT submit information that you consider to be confidential, or otherwise protected (such as a Social Security number or an unlisted phone number) or confidential business information that you do not want publicly disclosed. All comments may be posted on the

Internet and can be retrieved by most Internet search engines.

*For Further Information Contact:* Mr. Frank Gonzalez of the Department, telephone (202) 693-8553. (This is not a toll-free number.)

**Blue Cross and Blue Shield of Kansas City**

**Located in Kansas City, Missouri**

**[Application No. D-12039]**

**Proposed Exemption**

The Department is considering granting an exemption under the authority of Section 408(a) of the Employee Retirement Income Security Act of 1974, as amended (ERISA), and Section 4975(c)(2) of the Internal Revenue Code of 1986, as amended (the Code). The proposed exemption relates to legal actions and claims (the Claims) against Allianz Global Investors U.S. LLC (Allianz) and Aon Investments USA Inc. (Aon), that arose from certain losses incurred by the Non-Contributory Retirement Program for Certain Employees of Blue Cross and Blue Shield of Kansas City (the Plan) in the first quarter of 2020.<sup>11</sup>

This proposed exemption would permit the Plan sponsor, Blue Cross and Blue Shield of Kansas City (BCBS KC), to make a series of payments to the Plan, including the past payment of \$87,000,000 made to the Plan on September 9,

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<sup>11</sup> In proposing this exemption, the Department is not expressing an opinion regarding the merits of any Claim against Allianz and Aon, or whether the Plan's fiduciaries met their fiduciary duties with respect to Plan assets that are the subject of the Claims. Further, in proposing this exemption, the Department is not limiting any party's claim, demand and/or cause of action arising from the Plan's 2020 first quarter losses in any way. Among other things, this exemption preserves any right, claim, demand and/or cause of action the Plan may have against the following: (1) any fiduciary of the Plan; (2) any fiduciary of the Trust; (3) Blue Cross and Blue Shield of Kansas City; and/or (4) any person or entity related to a person or entity described in (1)-(3).

2021, and additional payments to the Plan totaling \$13,000,000 by December 31, 2024. If the Plan receives litigation proceeds from the Claims, the Plan will transfer the lesser of the litigation proceeds amount or the Restorative Payments amount already received by the Plan, plus reasonable attorney fees to BCBS KC.

### **SUMMARY OF FACTS AND REPRESENTATIONS<sup>12</sup>**

1. BCBS KC is a not-for-profit company that provides health insurance products and services. BCBS KC is an independent licensee of the Blue Cross Blue Shield Association (BCBSA).

2. The Plan is an ERISA-covered qualified defined benefit pension plan that covers eligible employees of BCBS KC and employees of affiliated employers. On June 30, 2013, the Plan was closed to new entrants. As of August 31, 2020, the Plan covered 1,212 participants and held \$80,441,432 in total assets.

3. The Plan holds a beneficial interest in the Blue Cross and Blue Shield National Retirement Trust (the

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<sup>12</sup> The Department notes that availability of this exemption is subject to the express condition that the material facts and representations contained in application D-12039 are true and complete at all times and accurately describe all material terms of the transactions covered by the exemption. If there is any material change in a transaction covered by the exemption or in a material fact or representation described in the application, the exemption will cease to apply as of the date of such change. The Summary of Facts and Representations is based on the Applicant's representations, as well as factual representations contained in the Claims' cause of action (as described below) and does not reflect factual findings or opinions of the Department, unless indicated otherwise.

Trust). The Trust is a master trust that holds the assets of 16 defined benefit pension plans that participate in the BCBSA's National Retirement Program (the Participating Plans). Northern Trust serves as Trustee and asset custodian to the Trust and maintains separate records that reflect the net asset value of each Participating Plan. The Trust's earnings, market adjustments, and administrative expenses are allocated among the Participating Plans based on the respective Participating Plan's share of the Trust's assets. A Participating Plan's interest in the Trust's net assets is based on its share of the Trust.

4. The Committee serves as named fiduciary and administrator for each Participating Plan. The Committee is a standing committee of the BCBSA's board of directors. In 2011, the Committee invested a portion of the Trust's assets in funds managed by Allianz Global Investors U.S. LLC (Allianz), as part of a Structured Alpha Investment Strategy. These funds included: (a) AllianzGI Structured Alpha Multi-Beta Series LLC I; (b) AllianzGI Structured Alpha Emerging Markets Equity 350 LLC; and (c) AllianzGI Structured Alpha 1000 LLC (collectively, the Structured Alpha Funds).

5. The Applicant represents that the Allianz Structured Alpha strategy consisted of alpha and beta components. According to the applicant, the alpha

component was an options trading strategy that Allianz claimed would seek targeted positive return potential while maintaining structural risk protections. The beta component was intended to provide broad market exposure to a particular asset class through investments in financial products similar to an exchange-traded fund that replicates the performance of a market index, such as the S&P 500. According to the Applicant, Allianz represented that the Structured Alpha Strategy would capitalize on the return-generating features of option selling (short volatility) while simultaneously benefitting from the risk-control attributes associated with option buying (long volatility). According to the Applicant, Allianz represented further that the alpha component would include position hedging consisting of long-volatility positions designed to protect the portfolio in the event of a market crash.

6. As of December 31, 2019, the total market value of the Plan's portion of the Trust's investment in the Allianz Structured Alpha Funds was \$170,800,689, which represented 77.66% of total Plan assets.<sup>13</sup>

7. In 2009, the Committee retained Aon (then called Ennis Knupp) to provide investment advice regarding the investment of Plan assets held in the Trust. The Applicant represents that Aon provided regular investment advice

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<sup>13</sup> By proposing this exemption, the Department does not, in any way, suggest a conclusion that the Plan's fiduciaries met their ERISA Section 404 duties when they caused the Trust to invest 77.66% of the Plan's total assets in the Allianz Structured Alpha Funds.

pursuant to a written contract between it and the Committee. Pursuant to its engagement, Aon agreed to provide the following: "recommendations to [the Committee] regarding asset allocation" within the Trust; "recommendations to [the Committee] regarding the specific asset allocation and other investment guidelines" for the Trust's investment managers such as Allianz; and advice "regarding the diversification of assets" held in the Trust." The Applicant represents that Aon agreed to: conduct "active, ongoing monitoring" of Allianz to "identify any forward-looking" risks "that could impact performance;" and "inform itself" of any information necessary to discharge its duty to monitor, including information about the actual options positions Allianz had constructed.

8. The Applicant represents that when equity markets sharply declined in February and March of 2020, volatility spiked and the options positions held within the Structured Alpha Strategy were exposed to a heightened risk of loss. The Applicant represents that, unbeknownst to the Committee, and in violation of Allianz's stated investment strategy, Allianz abandoned the hedging strategy that was the supposed cornerstone of the Structured Alpha Strategy, leaving the portfolio almost entirely unhedged against a spike in market volatility. As described in the Claims, although Allianz had represented that it would buy hedges



at strike prices ranging from 10% to 25% below the market, the hedges it actually held at the end of February 2020 were as much as 60% below the market.

The Applicant represents that, as of January 31, 2020, the Trust had invested approximately \$2,916,049,486 in the Structured Alpha Strategy. Six weeks later, the Trust faced a margin call, which the Applicant states left it no choice but to liquidate the investment. The Trust was ultimately able to redeem only \$646,762,678 of its \$2,916,049,486 investment, resulting in a total loss of \$2,269,286,808.

Specifically, regarding the Plan's portion of the loss, as of December 31, 2019 the market value of Plan assets was \$219,924,260. As of March 31, 2020, the market value of Plan assets decreased to \$73,641,344. The Applicant represents that the Plan's total losses from the Allianz Structured Alpha Strategy were \$139,613,178, which caused the Plan to be underfunded.

9. On September 16, 2020, the Committee filed a cause of action in the United States District Court for the Southern District of New York (Case number 20-CIV-07606) against Allianz and Aon for Breach of Fiduciary Duty under ERISA Section 404, Breach of Co-Fiduciary Duty under ERISA Section 405, and violation of ERISA Section 406(b) for managing the Plan assets in its self-interest and breach of contract. It is possible that resolution of this claim and

other legal actions against Allianz and Aon in connection with the Plan's losses (the Claims) could take an extended period of time.

10. The Applicant states that rather than wait for the Claims to be resolved, BCBS KC took steps to protect Plan benefits and avoid onerous benefit restrictions under Code section 436 that could apply to the Plan as a result of a funding shortfall. Therefore, on November 5, 2020, BCBS KC and the Plan entered into a Contribution and Assignment Agreement (the Contribution and Assignment Agreement).

11. Pursuant to the Contribution and Assignment Agreement, BCBS KC agreed to make \$100,000,000 in Restorative Payments to the Plan by September 30, 2021. On September 9, 2021, BCBS KC made an \$87,000,000 Restorative Payment to the Plan. Subsequently, on September 23, 2021, BCBS KC and the Plan amended the Restorative Payments provision of the Contribution and Assignment Agreement to state that BCBS KC will make \$100,000,000 in Restorative Payments to the Plan by December 31, 2024. The prior payment of \$87,000,000 together with the required future payment of \$13,000,000 constitutes the Required Restorative Payments under this exemption.

12. In exchange for the Restorative Payments, the Plan assigned to BCBS KC its right to retain certain litigation and/or settlement proceeds recovered from the

Claims (the Assigned Interests).<sup>14</sup> Per the assignment, once the Allianz/Aon litigation is resolved and if the Plan receives litigation proceeds from the Claims, the Plan will transfer to BCBS KC a repayment (the Repayment) that does not exceed the total Restorative Payments made by BCBS KC as of that date, plus reasonable attorney fees paid by BCBS KC on behalf of the Plan in connection with the Claims, if such fees are reviewed and approved by a qualified independent fiduciary who confirms that the fees were reasonably incurred and paid by BCBS KC to unrelated third parties (the Attorney Fees).

For the purposes of this exemption, Attorney Fees reimbursable to BCBS KC do not include: (a) legal expenses paid by the Plan; and (b) legal expenses paid by BCBS KC for representation of its own interests or the interests of any party other than the Plan. For purposes of determining the amount of Attorney Fees the Plan may reimburse to BCBS KC under this exemption, the amount of reasonable attorney fees paid by BCBS KC on behalf of the Plan in connection with the Claims must be reduced by the amount of legal fees received by BCBS KC in connection with the Claims from any non-Plan party (for example, from a third party pursuant to a court award).

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<sup>14</sup> Under the Contribution and Assignment Agreement, if the Plan receives litigation or settlement proceeds from the Claims, the proceeds would first flow to the Trust, and then each Plan's pro rata portion of the proceeds would be deposited into the individual trust funding that Plan.

13. The Plan must ultimately receive at least the full value of the promised Restorative Payments, minus the Attorney Fees. The Plan may ultimately receive more than the Restorative Payment amount required under the Contribution and Assignment Agreement. If the Plan receives litigation or settlement proceeds that exceed the amount of Restorative Payments that BCBS KC has made to the Plan, the Plan's Repayment to BCBS KC will be limited to the amount of Restorative Payments actually made by BCBS KC, plus Attorney Fees. For example, if BCBS KC has made \$100,000,000 in Restorative Payments to the Plan and has reasonably incurred \$100,000 in Attorney Fees, and if the Plan receives \$120,000,000 in litigation proceeds, the Plan will make a Repayment to BCBS KC totaling \$100,100,000.

14. Alternatively, if the Plan receives less litigation or settlement proceeds than the amount of Restorative Payments that BCBS KC has made to the Plan, the Plan will transfer to BCBS KC the lesser amount of litigation or settlement proceeds, plus Attorney Fees. For example, if BCBS KC has made \$100,000,000 in Restorative Payments to the Plan and has reasonably incurred \$100,000 in Attorney Fees, and if the Plan receives \$50,000,000 in litigation proceeds, the Plan will make a Repayment to BCBS KC totaling \$50,100,000.

15. The Department notes that if the Plan receives any restitution that is tied to the conduct underlying the

Claims but was ordered pursuant to a proceeding or directive that is external to Case number 20-CIV-07606, the disposition of such proceeds must conform to the requirements of this exemption.

16. BCBS KC retained Gallagher Fiduciary Advisors, LLC (Gallagher or the Independent Fiduciary) of New York, New York, to serve as the Plan's independent fiduciary with respect to the Required Restorative Payments and the potential repayment by the Plan of those Payments (collectively, the Proposed Transactions). Gallagher represents that it has extensive experience in institutional investment consulting and fiduciary decision-making regarding traditional and alternative investments. Gallagher further represents that its independent fiduciary decision-making work involves acting as a fiduciary advisor or decision-maker for plans and other ERISA-regulated asset pools and that it has experience with a wide range of asset classes and litigation claims.

17. Gallagher represents that it understands its duties and responsibilities under ERISA in acting as a fiduciary on behalf of the Plan. Gallagher also acknowledges that it is authorized to take all appropriate actions to safeguard the Plan's interests, and that it will monitor the Proposed Transactions on the Plan's behalf on a continuous basis and throughout the term required by this exemption.

18. Gallagher represents that it does not have any prior relationship with any parties in interest to the Plan, including BCBS KC and any BCBS KC affiliates. Gallagher further represents the total revenues it has received from the Plan and from parties in interest to the Plan in connection with its engagement as Independent Fiduciary represents approximately 0.78% of Gallagher's total revenue.

19. Gallagher represents that no party associated with this exemption application has or will indemnify it, in whole or in part, for negligence of any kind and/or any violation of state or federal law that may be attributable to Gallagher's performance of its duties as Independent Fiduciary to the Plan with respect to the Proposed Transactions. In addition, no contract or instrument entered into by Gallagher as Independent Fiduciary may purport to waive any liability under state or federal law for any such violation.

20. On November 5, 2020, Gallagher completed an Independent Fiduciary Report (the Independent Fiduciary Report) finding that the massive losses caused by the Trust's investment in the Allianz Structured Alpha Strategy resulted in a significant reduction to the Plan's total assets and funding level. Gallagher represents that the Required Restorative Payments, which will be received by the Plan substantially in advance of a final resolution of

the Claims against Allianz and Aon, should restore the Plan's funded percentage to its pre-loss funded percentage as of January 1, 2019. The restoration of the Plan's funding status will secure ongoing benefit payments to participants and beneficiaries.

Gallagher notes that the Contribution and Assignment Agreement provides that the Trust must reimburse BCBS KC only up to the Required Restorative Payment Amount by the Plan, plus any reasonable legal expense paid to non-BCBS KC-related parties that were incurred by, or allocated to, BCBS KC as a result of the Claims.<sup>15</sup> Thus, if the Plan's ultimate recovery amount from the Claims is less than the Required Restorative Payment Amount, plus related litigation expenses that were allocated to the Plan, BCBS KC, not the Plan, will suffer the loss.

Gallagher states that the Proposed Transactions and the terms of the Contribution and Assignment Agreement were negotiated and approved by Gallagher in its role as the Plan's Independent Fiduciary. Gallagher states that it approved the Proposed Transactions only after conducting an extensive analysis of the damages suffered by the Plan as a result of the failed Allianz Structured Alpha Strategy.

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<sup>15</sup> Currently, legal fees and expenses associated with the Claims are being paid by most of the Participating Plan's trusts on a pro rata basis according to each Participating Plan's total invested assets held in the Master Trust's Allianz Structured Alpha Strategy before the losses were incurred in the first quarter 2020. The Applicant represents that the Committee reviews and approves these legal fees before passing them through to each Participating Plan.

Gallagher represents that it conducted numerous discussions with Trust representatives and counsel, along with the Plan's representatives and counsel to ensure that the interests of the Plan's participants and beneficiaries were protected with respect to all aspects of the Proposed Transactions. Based upon its assessment, Gallagher approved the Plan's receipt of the Required Restorative Payments from BCBS KC in exchange for the Assignment.

#### ERISA Analysis

21. Absent an exemption, the Plan's receipt of the Restorative Payments from BCBS KC in exchange for the Plan's transfer of litigation or settlement proceeds to BCBS KC would violate ERISA. In this regard, ERISA Section 406(a)(1)(A) prohibits a plan fiduciary from causing the plan to engage in a transaction if the fiduciary knows or should know that such transaction constitutes a direct or indirect sale or exchange of any property between a plan and a party in interest. BCBS KC, as an employer whose employees are covered by the Plan, is a party in interest with respect to the Plan under ERISA Section 3(14)(C). The Required Restorative Payments to the Plan and the Plan's potential repayment to BCBS KC with litigation or settlement proceeds would constitute impermissible exchanges between the Plan and a party-in-interest (BCBS KC) in violation of ERISA Section 406(a)(1)(A).



ERISA Section 406(a)(1)(B) prohibits the lending of money or other extension of credit between a plan and a party-in-interest. BCBS KC's promise to make additional Required Restorative Payments to the Plan, over time, constitutes an impermissible extension of credit between the Plan and a party-in-interest in violation of ERISA Section 406(a)(1)(B).

ERISA Section 406(a)(1)(D) prohibits a plan fiduciary from causing a plan to engage in a transaction if the fiduciary knows or should know that the transaction constitutes a direct or indirect transfer to, or use by or for the benefit of, a party-in-interest, of the income or assets of the plan. The transfer of Plan assets to BCBS KC in connection with the Repayment would constitute an impermissible transfer of Plan assets to a party-in-interest in violation of ERISA Section 406(a)(1)(D).

#### Conditions

22. This proposed exemption contains a number of conditions that must be met. For example, the proposed exemption mandates that the Independent Fiduciary, in full accordance with its obligations of prudence and loyalty under ERISA Section 404(a)(1)(A) and (B) must:

(a) review, negotiate, and approve the terms and conditions of the Required Restorative Payments, the Repayment, and the Contribution and Assignment Agreement,

before the Plan enters into such payments and the agreement;

(b) determine that the terms and conditions of the Required Restorative Payments, the Repayment, and the Contribution and Assignment Agreement are prudent, in the interest of the Plan and its participants and beneficiaries, and protective of the rights of the Plan's participants and beneficiaries;

(c) confirm that the Required Restorative Payments are fully and timely made;

(d) monitor the Claims and confirm that the Plan receives its proper share of any litigation or settlement proceeds received by the Trust in connection with the Claims;

(e) ensure that any Repayment by the Plan to BCBS KC fully complies with the terms of this exemption and is for no more than the lesser of the total Restorative Payments actually made to the Plan by BCBS KC or the amount the Plan received from the Claims, plus Attorney Fees;

(f) ensure that any Repayment by the Plan to BCBS KC for legal expenses in connection with the Claims is limited to only reasonable legal expenses that were paid by BCBS KC to unrelated third parties for representation of the Plan and its interests (as opposed to representation of BCBS KC or the interests of any party other than the Plan) where BCBS KC was not otherwise reimbursed from a non-Plan party;

(g) monitor the Plan's Assigned Interests on an ongoing basis to determine and confirm that any excess recovery amount from the Claims (i.e., any amount that exceeds the Required Restorative Payment Amount) is retained by the Plan;

(h) ensure that all of the conditions and definitions of this proposed exemption are met; and

(i) represent that it has not and will not enter into any agreement or instrument that violates ERISA Section 410 or Department Regulations codified at 29 CFR section 2509.75-4.<sup>16</sup>

23. This proposed exemption also requires Gallagher to respond in writing to any information requests from the Department regarding Gallagher's activities as the Plan's Independent Fiduciary. Additionally, no later than 90 days after the resolution of the litigation, Gallagher must submit a written report to the Department demonstrating that all terms and conditions of the exemption have been met.

24. This proposed exemption requires that the Plan has not and will not release any claims, demands and/or causes of action it may have against: (a) any fiduciary of the Plan; (b) any fiduciary of the Trust; (c) BCBS KC;

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<sup>16</sup> ERISA Section 410 provides, in part, that "except as provided in ERISA Sections 405(b)(1) and 405(d), any provision in an agreement or instrument which purports to relieve a fiduciary from responsibility or liability for any responsibility, obligation, or duty under this part [meaning Part 4 of Title I of ERISA] shall be void as against public policy."

and/or (d) any person or entity related to a person or entity described in (a)-(c) of this paragraph.

Additionally, any Repayment by the Plan to BCBS KC must be made in a manner designed to minimize unnecessary costs and disruption to the Plan and its investments.

25. The Plan may not make any Repayment to BCBS KC before the date: the Plan has received from BCBS KC the entire amount of the Restorative Payments agreed to in the Amended Contribution and Assignment Agreement; and all the Claims are settled. Furthermore, the Plan may not pay any interest to BCBS KC in connection with its receipt of the Required Restorative Payments, nor pledge Plan assets to secure any portion of the Required Restorative Payments.

26. Pursuant to this proposed exemption, the Plan may not incur any expenses, commissions or transaction costs in connection with the Proposed Transactions. However, as noted above, under certain circumstances the Plan may reimburse BCBS KC for reasonable legal expenses arising from the Claims that BCBS KC paid to non-BCBS KC-related parties for representation of the Plan and its interests (as opposed to representation of BCBS KC or the interests of any party other than the Plan) where BCBS KC was not otherwise reimbursed by a non-Plan party.

27. Finally, the exemptive relief provided under this proposed exemption is conditioned upon the Department's assumption that the material facts and representations set

forth above in the Summary of Facts and Representation section are true and accurate at all times. In the event that a material fact or representation detailed above is untrue or inaccurate, the exemptive relief provided under this exemption will cease immediately.

### Statutory Findings

28. ERISA Section 408(a) provides, in part, that the Department may not grant an exemption unless the Department finds that the exemption is administratively feasible, in the interest of affected plans and of their participants and beneficiaries, and protective of the rights of such participants and beneficiaries. Each of these criteria is discussed below.

a. The Proposed Exemption Is "Administratively Feasible." The Department has tentatively determined that the proposed exemption is administratively feasible because, among other things, the Independent Fiduciary will represent the interests of the Plan for all purposes with respect to the Proposed Transactions.<sup>17</sup> In this regard, not later than 90 days after the resolution of the litigation, the Independent Fiduciary must submit a written report to the

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<sup>17</sup> This proposed exemption would require that if the Independent Fiduciary resigns, is removed, or for any reason is unable to serve as an Independent Fiduciary, the successor Independent Fiduciary must, among other things, assume all of the duties of the outgoing Independent Fiduciary. As soon as possible, including before the appointment of a successor Independent Fiduciary, the Plan Sponsor and the Plan must notify the Department's Office of Exemption Determinations of the change in Independent Fiduciaries. The notification must contain all material information including the qualifications of the successor Independent Fiduciary.

Department demonstrating that all of the requirements of this exemption have been met.

b. The Proposed Exemption Is "In the Interests of the Plan." The Department has tentatively determined that the proposed exemption is in the interest of the Plan because, among other things, the Plan's receipt of the Required Restorative Payments will substantially improve the Plan's funding status, which will enhance the Plan's ability to meet its obligations to fund benefit obligations to participants and beneficiaries and help the Plan avoid the imposition of benefit limitations imposed under Code section 436.

c. The Proposed Exemption Is "Protective of the Plan." The Department has tentatively determined that the proposed exemption is protective of the rights of the Plan's participants and beneficiaries because, among other things, the Plan will repay BCBS KC the lesser of the Required Restorative Payment Amount, or the amount the Plan receives in proceeds from the Claims, ensuring that the Proposed Transactions will result in an increase in Plan assets of at least the total amount of Restorative Payments (less reasonable legal expenses related to the Claims paid by BCBS KC to unrelated third parties, as confirmed and approved by the Independent Fiduciary). Further, this exemption preserves any right, claim, demand and/or cause of action the Plan may have against: (a) any fiduciary of the Plan;

(b) any fiduciary of the Trust; (c) BCBS KC; and/or (d) any person or entity related to a person or entity described in (a) - (c).

### Summary

29. Based on the conditions described above, the Department has tentatively determined that the relief sought by the Applicant satisfies the statutory requirements under ERISA Section 408(a) for the Department to make findings that support its issuance of a proposed exemption.

### **PROPOSED EXEMPTION**

The Department is considering granting an exemption under the authority of ERISA Section 408(a) and Code Section 4975(c)(2) and in accordance with the procedures set forth in the Department's exemption procedure regulation.<sup>18</sup>

### **Section I. Definitions**

(a) The term "Attorney Fees" means reasonable legal expenses paid by BCBS KC on behalf of the Plan in connection with the Claims, if such fees are reviewed and approved by a qualified independent fiduciary who confirms that the fees were reasonably incurred and paid by BCBS KC to unrelated third parties. For the purposes of this

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<sup>18</sup> 29 CFR part 2570, subpart B (55 FR 32836, 32847, August 10, 1990).

exemption, the Attorney Fees reimbursable to BCBS KC do not include: (1) legal expenses paid by the Plan; and (2) legal expenses paid by BCBS KC for representation of BCBC KC or the interests of any party other than the Plan.

(b) The term "BCBS KC" means Blue Cross and Blue Shield of Kansas City.

(c) The term "Claims" means the legal claims against Allianz Global Investors U.S. LLC (Allianz) and Aon Investments USA Inc. (Aon), to recover certain losses incurred by the Plan in the first quarter of 2020.

(d) The term "Contribution and Assignment Agreement" means the written agreement between BCBS KC and the Plan, dated November 5, 2020, and its amendment that became effective on September 23, 2021, containing all material terms regarding BCBS KC's agreement to make Required Restorative Payments to the Plan in return for the Plan's potential Repayment to BCBS KC of an amount that is no more than lesser of the Required Restorative Payment Amount (as described in Section I(h)) or the amount of litigation proceeds the Plan receives from the Claims, plus reasonable attorney fees paid to unrelated third parties by BCBS KC in connection with the Claims.

(e) The term "Independent Fiduciary" means Gallagher Fiduciary Advisors, LLC (Gallagher) or a successor Independent Fiduciary to the extent Gallagher or the



successor Independent Fiduciary continues to serve in such capacity who:

(1) Is not an affiliate of BCBS KC and does not hold an ownership interest in BCBS KC or affiliates of BCBS KC;

(2) Was not a fiduciary with respect to the Plan before its appointment to serve as the Independent Fiduciary;

(3) Has acknowledged in writing that it:

(i) is a fiduciary with respect to the Plan and has agreed not to participate in any decision regarding any transaction in which it has an interest that might affect its best judgment as a fiduciary; and

(ii) Has appropriate technical training or experience to perform the services contemplated by the exemption;

(4) Has not entered into any agreement or instrument that violates the prohibitions on exculpatory provisions in ERISA Section 410 or the Department's regulation relating to indemnification of fiduciaries;<sup>19</sup>

(5) Has not received gross income from BCBS KC or its affiliates during any fiscal year in an amount that exceeds two percent (2%) of the Independent Fiduciary's gross income from all sources for the prior fiscal year. This provision also applies to a partnership or corporation

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<sup>19</sup> 29 CFR 2509.75-4.

of which the Independent Fiduciary is an officer, director, or 10 percent (10%) or more partner or shareholder, and includes as gross income amounts received as compensation for services provided as an independent fiduciary under any prohibited transaction exemption granted by the Department; and

(6) No organization or individual that is an Independent Fiduciary, and no partnership or corporation of which such organization or individual is an officer, director, or ten percent (10%) or more partner or shareholder, may acquire any property from, sell any property to, or borrow any funds from BCBS KC or from affiliates of BCBS KC while serving as an Independent Fiduciary. This prohibition will continue for six months after the party ceases to be an Independent Fiduciary and/or the Independent Fiduciary negotiates any transaction on behalf of the Plan during the period that the organization or individual serves as an Independent Fiduciary.

(f) The "Plan" means the Non-Contributory Retirement Program for Certain Employees of Blue Cross and Blue Shield of Kansas City.

(g) The term "Plan Losses" means the \$139,613,178 in Plan losses the BCBSA's National Employee Benefits Committee alleges were the result of breaches of fiduciary

responsibilities and breaches of contract by Allianz Global Investors U.S. LLC and/or Aon Investments USA Inc.

(h) The term "Restorative Payments" means the payments made by BCBS KC to the Plan in connection with the Plan Losses, defined above, consisting of: (1) the past payment of \$87,000,000 on September 9, 2021; and (2) a second installment amount of \$13,000,000 due to the Plan by December 31, 2024. The sum of (1) and (2) is the Required Restorative Payment Amount.

(i) The "Repayment" means the payment, if any, that the Plan will transfer to BCBS KC following the Plan's receipt of proceeds from the Claims, where the Repayment is made following the full and complete resolution of the Claims; and in a manner that is consistent with the terms of the exemption.

## **Section II. Proposed Transactions**

If the proposed exemption is granted, the restrictions of ERISA Sections 406(a)(1)(A), (B) and (D) and the sanctions resulting from the application of Code Section 4975, by reason of Code Sections 4975(c)(1)(A), (B) and (D), shall not apply, effective November 5, 2020, to the following transactions: BCBS KC's transfer of Restorative Payments to the Plan; and, in return, the Plan's Repayment of an amount to BCBS KC, which must be no more than the lesser of the Restorative Payment or the amount of

litigation proceeds the Plan received from the Claims, plus reasonable Attorney Fees, provided that the Definitions set forth in Section I and the Conditions set forth in Section III are met.

**Section III. Conditions**

(a) The Plan receives the entire Restorative Payment Amount no later than December 31, 2024;

(b) In connection with its receipt of the Required Restorative Payments, the Plan does not release any claims, demands and/or causes of action the Plan may have against the following: (1) any fiduciary of the Plan; (2) any fiduciary of the Trust; (3) BCBS KC; and/or (4) any person or entity related to a person or entity identified in (1)-(3) of this paragraph;

(c) The Plan's Repayment to BCBS KC is for no more than the lesser of the total Restorative Payments received by the Plan or the amount of litigation proceeds the Plan receives from the Claims. The Plan's Repayment to BCBS KC may only occur after the Independent Fiduciary has determined that: all the conditions of the exemption are met; the Plan has received all the Restorative Payments it is due; and the Plan has received all the litigation proceeds it is due. The Plan's Repayment to BCBS KC must be carried out in a manner designed to minimize unnecessary costs and disruption to the Plan and its investments;

(d) A qualified independent fiduciary (the Independent Fiduciary, as further defined in Section II(e)), acting solely on behalf of the Plan in full accordance with its obligations of prudence and loyalty under ERISA Sections 404(a)(1)(A) and (B) must:

(1) Review, negotiate and approve the terms and conditions of the Restorative Payments and the Repayment and the Contribution and Assignment Agreement, all of which must be in writing, before the Plan enters into those transactions/agreement;

(2) Determine that the Restorative Payments, the Repayment, and the terms of the Contribution and Assignment Agreement, are prudent and in the interest of the Plan and its participants and beneficiaries;

(3) Confirm that the Required Restorative Payment Amount was fully and timely made;

(4) Monitor the litigation related to the Claims and confirm that the Plan receives, in a timely manner, its proper share of any litigation or settlement proceeds received by the Trust;

(5) Ensure that any Repayment by the Plan to BCBS KC for legal expenses in connection with the Claims is limited to only reasonable legal expenses that were paid by BCBS KC to unrelated third parties;

(6) Ensure that all of the conditions and definitions of this proposed exemption are met;

(7) Submit a written report to the Department's Office of Exemption Determinations demonstrating and confirming that the terms and conditions of the exemption were met, within 90 days after the Repayment; and

(8) Not enter into any agreement or instrument that violates ERISA Section 410 or the Department's Regulations codified at 29 CFR Section 2509.75-4.

(f) The Plan pays no interest in connection with the Restorative Payments;

(g) The Plan does not pledge any Plan assets to secure any portion of the Restorative Payments;

(h) The Plan does not incur any expenses, commissions, or transaction costs in connection with the Proposed Transactions. However, if first approved by the Independent Fiduciary, the Plan may reimburse BCBS KC for reasonable legal expenses paid in connection with the Claims by BCBS KC to non-BCBS KC-related parties. For purposes of determining the amount of Attorney Fees the Plan may reimburse to BCBS KC under this proposal, the amount of reasonable attorney fees paid by BCBS KC on behalf of the Plan in connection with the Claims must be reduced by the amount of legal fees received by BCBS KC in connection with the Claims from any non-Plan party (i.e., pursuant to a court award);

(i) The proposed transactions do not involve any risk of loss to either the Plan or the Plan's participants and beneficiaries;

(j) No party associated with this exemption has or will indemnify the Independent Fiduciary and the Independent Fiduciary will not request indemnification from any party, in whole or in part, for negligence and/or any violation of state or federal law that may be attributable to the Independent Fiduciary in performing its duties to the Plan with respect to the Proposed Transactions. In addition, no contract or instrument may purport to waive any liability under state or federal law for any such violation.

(k) If an Independent Fiduciary resigns, is removed, or for any reason is unable to serve as an Independent Fiduciary, the Independent Fiduciary must be replaced by a successor entity that: (1) meets the definition of Independent Fiduciary detailed above in Section II(e); and (2) otherwise meets all of the qualification, independence, prudence and diligence requirements set forth in this exemption. Further, any such successor Independent Fiduciary must assume all of the duties of the outgoing Independent Fiduciary. As soon as possible, including before the appointment of a successor Independent Fiduciary, BCBS KC must notify the Department's Office of Exemption Determinations of the change in Independent

Fiduciary and such notification must contain all material information regarding the successor Independent Fiduciary, including the successor Independent Fiduciary's qualifications; and

(1) All of the material facts and representations set forth in the Summary of Facts and Representation are true and accurate at all times.

#### NOTICE TO INTERESTED PERSONS

The Applicant will give notice of the proposed exemption to all interested persons and all of the parties to the litigation described above, within fifteen calendar days after the publication of the notice of proposed exemption in the *Federal Register*. The notice will contain a copy of the notice of proposed exemption, as published in the *Federal Register*, and a supplemental statement, as required pursuant to the Department's regulations codified at 29 CFR 2570.43(a)(2). The supplemental statement will inform interested persons of their right to comment on the pending exemption. Written comments are due by [INSERT DATE THAT IS 45 DAYS FROM THE PUBLICATION OF THE NOTICE IN THE *FEDERAL REGISTER*].

All comments will be made available to the public.

**Warning:** If you submit a comment, EBSA recommends that you include your name and other contact information in the body of your comment, but DO NOT submit information that you



consider to be confidential, or otherwise protected (such as a Social Security number or an unlisted phone number) or confidential business information that you do not want publicly disclosed. All comments may be posted on the Internet and can be retrieved by most Internet search engines.

*For Further Information Contact:* Mr. Nicholas Schroth of the Department, telephone (202) 693-8571. (This is not a toll-free number.)

**Blue Cross and Blue Shield of Arizona, Inc.**

**Located in Phoenix, Arizona**

**[Application No. D-12035]**

### **Proposed Exemption**

The Department is considering granting an exemption under the authority of Section 408(a) of the Employee Retirement Income Security Act of 1974, as amended (ERISA), and Section 4975(c)(2) of the Internal Revenue Code of 1986, as amended (the Code). The proposed exemption relates to legal actions and claims (the Claims) against Allianz Global Investors U.S. LLC (Allianz) and Aon Investments USA Inc. (Aon), that arose from certain losses incurred by the Non-Contributory Retirement Program for Certain Employees of Blue Cross and Blue Shield of Arizona, Inc. (the Plan) in the first quarter of 2020.<sup>20</sup>

This proposed exemption would permit the Plan sponsor, Blue Cross and Blue Shield of Arizona, Inc. (BCBS AZ), to make a series of payments to the Plan, including:

(a) past payments totaling \$130,000,000; and (b) future

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<sup>20</sup> In proposing this exemption, the Department is not expressing an opinion regarding the merits of any Claim against Allianz and Aon, or whether the Plan's fiduciaries met their fiduciary duties with respect to Plan assets that are the subject of the Claims. Further, in proposing this exemption, the Department is not limiting any party's claim, demand and/or cause of action arising from the Plan's 2020 first quarter losses in any way. Among other things, this exemption preserves any right, claim, demand and/or cause of action the Plan may have against the following: (1) any fiduciary of the Plan; (2) any fiduciary of the Trust; (3) the Blue Cross and Blue Shield of Arizona, Inc.; and/or (4) any person or entity related to a person or entity described in (1)-(3).

amounts necessary for (i) the Plan's assets to be equal to or greater than 100% of the Plan's current liabilities, and (ii) the Plan to have an adjusted funding target attainment percentage (AFTAP) of 110% (the Restorative Payments).

If the Plan receives litigation proceeds from the Claims, the Plan will transfer the lesser of the litigation proceeds amount or the Restorative Payments, plus reasonable attorney fees to BCBS AZ.

#### **SUMMARY OF FACTS AND REPRESENTATIONS<sup>21</sup>**

1. Blue Cross and Blue Shield of Arizona, Inc. (BCBS AZ or the Applicant) is a not-for-profit company that provides health insurance products and services. BCBS AZ is an independent licensee of the Blue Cross Blue Shield Association (BCBSA).

2. The Plan is an ERISA-covered qualified defined benefit pension plan that covers eligible employees of BCBS AZ and employees of affiliated employers. On June 30, 2012, the Plan was closed to new entrants. As of August 31, 2020, the Plan held \$178,703,160 in total assets.

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<sup>21</sup> The Department notes that availability of this exemption is subject to the express condition that the material facts and representations contained in application D-12035 are true and complete at all times and accurately describe all material terms of the transactions covered by the exemption. If there is any material change in a transaction covered by the exemption or in a material fact or representation described in the application, the exemption will cease to apply as of the date of such change. The Summary of Facts and Representations is based on the Applicant's representations, as well as factual representations contained in the Claims' cause of action (as described below) and does not reflect factual findings or opinions of the Department, unless indicated otherwise.

3. The Plan holds a beneficial interest in the Blue Cross and Blue Shield National Retirement Trust (the Trust). The Trust is a master trust that holds the assets of 16 defined benefit pension plans that participate in the BCBSA's National Retirement Program (the Participating Plans). Northern Trust serves as Trustee and asset custodian to the Trust and maintains separate records that reflect the net asset value of each Participating Plan. The Trust's earnings, market adjustments, and administrative expenses are allocated among the Participating Plans based on the respective Participating Plan's share of the Trust's assets. A Participating Plan's interest in the Trust's net assets is based on its share of the Trust.

4. The Committee serves as named fiduciary and administrator for each Participating Plan. The Committee is a standing committee of the BCBSA's board of directors. In 2011, the Committee invested a portion of the Trust's assets in funds managed by Allianz Global Investors U.S. LLC (Allianz), as part of a Structured Alpha Investment Strategy. These funds included: (a) AllianzGI Structured Alpha Multi-Beta Series LLC I; (b) AllianzGI Structured Alpha Emerging Markets Equity 350 LLC; and (c) AllianzGI Structured Alpha 1000 LLC (collectively, the Structured Alpha Funds).

5. The Applicant represents that the Allianz Structured Alpha strategy consisted of alpha and beta components. According to the applicant, the alpha component was an options trading strategy that Allianz claimed would seek targeted positive return potential while maintaining structural risk protections. The beta component was intended to provide broad market exposure to a particular asset class through investments in financial products similar to an exchange-traded fund that replicates the performance of a market index, such as the S&P 500. According to the Applicant, Allianz represented that the Structured Alpha Strategy would capitalize on the return-generating features of option selling (short volatility) while simultaneously benefitting from the risk-control attributes associated with option buying (long volatility). According to the Applicant, Allianz represented further that the alpha component would include position hedging consisting of long-volatility positions designed to protect the portfolio in the event of a market crash.

6. As of December 31, 2019, the total market value of the Plan's portion of the Trust's investment in the Allianz Structured Alpha Funds was \$369.3 million, which represented 77.67% of total Plan assets.<sup>22</sup>

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<sup>22</sup> By proposing this exemption, the Department does not, in any way, suggest a conclusion that the Plan's fiduciaries met their ERISA Section 404 duties when they caused the Trust to invest 77.67% of the Plan's total assets in the Allianz Structured Alpha Funds.

7. In 2009, the Committee retained Aon (then called Ennis Knupp) to provide investment advice regarding the investment of Plan assets held in the Trust. The Applicant represents that Aon provided regular investment advice pursuant to a written contract between it and the Committee. Pursuant to its engagement, Aon agreed to provide the following: "recommendations to [the Committee] regarding asset allocation" within the Trust; "recommendations to [the Committee] regarding the specific asset allocation and other investment guidelines" for the Trust's investment managers such as Allianz; and advice "regarding the diversification of assets" held in the Trust." The Applicant represents that Aon agreed to: conduct "active, ongoing monitoring" of Allianz to "identify any forward-looking" risks "that could impact performance;" and "inform itself" of any information necessary to discharge its duty to monitor, including information about the actual options positions Allianz had constructed.

8. The Applicant represents that when equity markets sharply declined in February and March of 2020, volatility spiked and the options positions held within the Structured Alpha Strategy were exposed to a heightened risk of loss. The Applicant represents that, unbeknownst to the Committee, and in violation of Allianz's stated investment strategy, Allianz abandoned the hedging strategy that was

the supposed cornerstone of the Structured Alpha Strategy, leaving the portfolio almost entirely unhedged against a spike in market volatility. As described in the Claims, although Allianz had represented that it would buy hedges at strike prices ranging from 10% to 25% below the market, the hedges it actually held at the end of February 2020 were as much as 60% below the market.

The Applicant represents that, as of January 31, 2020, the Trust had invested approximately \$2,916,049,486 in the Structured Alpha Strategy. Six weeks later, the Trust faced a margin call, which the Applicant states left it no choice but to liquidate the investment. The Trust was ultimately able to redeem only \$646,762,678 of its \$2,916,049,486 investment, resulting in a total loss of \$2,269,286,808.

Specifically, regarding the Plan's portion of the loss, as of December 31, 2019, the market value of the Plan and its Code section 401(h) Account were \$416,127,759 and \$59,347,737, respectively.<sup>23</sup> As of March 31, 2020, the market value of the Plan's total assets and the Code section 401(h) Account decreased to \$137,298,008 and \$20,433,430, respectively. The Applicant represents that the Plan's total losses from the Allianz Structured Alpha

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<sup>23</sup> Code Section 401(h) permits a pension or annuity plan to provide for payment of benefits for sickness, accident, hospitalization and medical expenses for retired employees, their spouses and dependents. In order for the pension or annuity plan to meet the provisions of Code Section 401(h), the medical benefits must be subordinate to pension benefits and must be established and maintained in a separate account.

Strategy were \$302,470,379, which caused the Plan to be underfunded.

9. On September 16, 2020, the Committee filed a cause of action in the United States District Court for the Southern District of New York (Case number 20-CIV-07606) against Allianz and Aon for Breach of Fiduciary Duty under ERISA Section 404, Breach of Co-Fiduciary Duty under ERISA Section 405, and violation of ERISA Section 406(b) for managing the Plan assets in its self-interest and breach of contract. It is possible that resolution of this claim and other legal actions against Allianz and Aon in connection with the Plan's losses (the Claims) could take an extended period of time.

10. The Applicant states that rather than wait for the Claims to be resolved, BCBS AZ took steps to protect Plan benefits and avoid onerous benefit restrictions under Code section 436 that could apply to the Plan as a result of a funding shortfall. Therefore, on November 5, 2020, BCBS AZ and the Plan entered into a Contribution and Assignment Agreement (the Contribution and Assignment Agreement).

11. Pursuant to the Contribution and Assignment Agreement, BCBS AZ agreed to make \$274 million in Restorative Payments to the Plan pursuant to an installment payment structure (the Restorative Payments). BCBS AZ made its first installment payment of \$60 million to the Plan on



September 15, 2020. Thereafter, BCBS AZ made a Restorative Payment to the Plan of \$35,000,000 on December 28, 2020, and \$10,000,000 on July 31, 2021. Thus, as of July 31, 2021, BCBS AZ had made Restorative Payments to the Plan totaling \$105 million.

12. On October 13, 2021, BCBS AZ and the Plan amended the Restorative Payments provision of the Contribution and Assignment Agreement (the Restorative Payment Amendment). BCBS AZ agreed that before December 31, 2023, it would contribute amounts necessary for the Plan to have: (a) an adjusted funding target attainment percentage of 110% (after taking into account any waivers of the funding standard carryover balance by the Plan Sponsor); and (b) an amount of assets that is at least 100% of current Plan liabilities. In addition, any minimum required contributions made by BCBS AZ to the Plan on or after October 13, 2021, will not be included as part of the Restorative Payments required under the Contribution and Assignment Agreement. The prior restorative payments noted above in paragraph 11 together with the obligations noted here in paragraph 12 constitute the Required Restorative Payments under this exemption.

13. On December 21, 2021, BCBS AZ made a fourth Restorative Payment to the Plan totaling \$25,000,000.<sup>24</sup> The

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<sup>24</sup> With the \$25,000,000 payment, total Restorative Payments to the Plan now total \$130,000,000.

Applicant represents that after making this most recent \$25,000,000 Restorative Payment, BCBS AZ has brought the Plan's funding level to 110% of AFTAP and, thus, has met its obligation under item (a) of the Restorative Payment Amendment identified above. This exemption, if granted, requires BCBS AZ to make additional Restorative Contributions to the Plan before December 31, 2023, to ensure that the Plan has an amount of assets that is at least 100% of current Plan liabilities.

14. In exchange for the Restorative Payments, the Plan assigned to BCBS AZ its right to retain certain litigation and/or settlement proceeds recovered from the Claims (the Assigned Interests).<sup>25</sup> Per the assignment, once the Allianz/Aon litigation is resolved and if the Plan receives litigation proceeds from the Claims, the Plan will transfer to BCBS AZ a repayment (the Repayment) that does not exceed the total Restorative Payments made by BCBS AZ, plus reasonable attorney fees paid by BCBS AZ on behalf of the Plan in connection with the Claims, if such fees are reviewed and approved by a qualified independent fiduciary who confirms that the fees were reasonably incurred and paid by BCBS AZ to unrelated third parties (the Attorney Fees). For the purposes of this exemption, Attorney Fees

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<sup>25</sup> Under the Contribution and Assignment Agreement, if the Plan receives litigation or settlement proceeds from the Claims, the proceeds would first flow to the Trust, and then each Plan's pro rata portion of the proceeds would be deposited into the individual trust funding that Plan.

reimbursable to BCBS AZ do not include: (a) legal expenses paid by the Plan; and (b) legal expenses paid by BCBS AZ for representation of its own interests or the interests of any party other than the Plan. For purposes of determining the amount of Attorney Fees the Plan may reimburse to BCBS AZ under this exemption, the amount of reasonable attorney fees paid by BCBS AZ on behalf of the Plan in connection with the Claims must be reduced by the amount of legal fees received by BCBS AZ in connection with the Claims from any non-Plan party (for example, from a third party pursuant to a court award).

15. The Plan must ultimately receive at least the full value of the promised Restorative Payments, minus the Attorney Fees. The Plan may ultimately receive more than the Restorative Payment amount required under the Contribution and Assignment Agreement. If the Plan receives litigation or settlement proceeds that exceed the amount of Restorative Payments that BCBS AZ has made to the Plan, the Plan's Repayment to BCBS AZ will be limited to the amount of Restorative Payments actually made by BCBS AZ, plus Attorney Fees. For example, if BCBS AZ has made \$130,000,000 in Restorative Payments to the Plan and reasonably incurred \$100,000 in Attorney Fees, and the Plan receives \$160,000,000 in litigation proceeds, the Plan will make a Repayment to BCBS AZ totaling \$130,100,000.

16. Alternatively, if the Plan receives less litigation or settlement proceeds than the amount of Restorative Payments that BCBS AZ has made to the Plan, the Plan will transfer to BCBS AZ the lesser amount of litigation or settlement proceeds, plus Attorney Fees. For example, if BCBS AZ has made \$130,000,000 in Restorative Payments to the Plan and has reasonably incurred \$100,000 in Attorney Fees, and the Plan receives \$50,000,000 in litigation proceeds, the Plan will make a Repayment to BCBS AZ totaling \$50,100,000.

17. The Department notes that if the Plan receives any restitution that is tied to the conduct underlying the Claims but was ordered pursuant to a proceeding or directive that is external to Case number 20-CIV-07606, the disposition of such proceeds must conform to the requirements of this exemption.

18. BCBS AZ retained Gallagher Fiduciary Advisors, LLC (Gallagher or the Independent Fiduciary) of New York, New York, to serve as the Plan's independent fiduciary with respect to the Required Restorative Payments and the potential repayment by the Plan of those Payments (collectively, the Proposed Transactions). Gallagher represents that it has extensive experience in institutional investment consulting and fiduciary decision-making regarding traditional and alternative investments. Gallagher further represents that its independent fiduciary

decision-making work involves acting as a fiduciary advisor or decision-maker for plans and other ERISA-regulated asset pools and that it has experience with a wide range of asset classes and litigation claims.

19. Gallagher represents that it understands its duties and responsibilities under ERISA in acting as a fiduciary on behalf of the Plan. Gallagher also acknowledges that it is authorized to take all appropriate actions to safeguard the Plan's interests, and that it will monitor the Proposed Transactions on the Plan's behalf on a continuous basis and throughout the term required by this exemption.

20. Gallagher represents that it does not have any prior relationship with any parties in interest to the Plan, including BCBS AZ and any BCBS AZ affiliates. Gallagher further represents the total revenues it has received from the Plan and from parties in interest to the Plan in connection with its engagement as Independent Fiduciary represents approximately 0.78% of Gallagher's total revenue.

21. Gallagher represents that no party associated with this exemption application has or will indemnify it, in whole or in part, for negligence of any kind and/or any violation of state or federal law that may be attributable to Gallagher's performance of its duties as Independent Fiduciary to the Plan with respect to the Proposed

Transactions. In addition, no contract or instrument entered into by Gallagher as Independent Fiduciary may purport to waive any liability under state or federal law for any such violation.

22. On November 3, 2020, Gallagher completed an Independent Fiduciary Report (the Independent Fiduciary Report) finding that the massive losses caused by the Trust's investment in the Allianz Structured Alpha Strategy resulted in a significant reduction to the Plan's total assets and funding level. Gallagher represents that the Required Restorative Payments, which will be received by the Plan substantially in advance of a final resolution of the Claims against Allianz and Aon, should restore the Plan's funded percentage to its pre-loss funded percentage as of January 1, 2019. The restoration of the Plan's funding status will secure ongoing benefit payments to participants and beneficiaries.

Gallagher notes that the Contribution and Assignment Agreement provides that the Trust must reimburse BCBS AZ only up to the Required Restorative Payment Amount, plus any reasonable legal expense paid to non-BCBS AZ-related parties that were incurred by, or allocated to, BCBS AZ as a result of the Claims.<sup>26</sup> Thus, if the Plan's ultimate

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<sup>26</sup> Currently, legal fees and expenses associated with the Claims are being paid by most of the Participating Plan's trusts on a pro rata basis according to each Participating Plan's total invested assets held in the Master Trust's Allianz Structured Alpha Strategy before the losses were incurred in the first quarter 2020. The Applicant

recovery amount from the Claims is less than the Required Restorative Payment Amount, plus related litigation expenses that were allocated to the Plan, BCBS AZ, not the Plan, will suffer the loss.

Gallagher states that the Proposed Transactions and the terms of the Contribution and Assignment Agreement were negotiated and approved by Gallagher in its role as the Plan's Independent Fiduciary. Gallagher states that it approved the Proposed Transactions only after conducting an extensive analysis of the damages suffered by the Plan as a result of the failed Allianz Structured Alpha Strategy. Gallagher represents that it conducted numerous discussions with Trust representatives and counsel, along with the Plan's representatives and counsel to ensure that the interests of the Plan's participants and beneficiaries were protected with respect to all aspects of the Proposed Transactions. Based upon its assessment, Gallagher approved the Plan's receipt of the Required Restorative Payments from BCBS AZ in exchange for the Assignment.

#### ERISA Analysis

23. Absent an exemption, the Plan's receipt of the Restorative Payments from BCBS AZ in exchange for the Plan's transfer of litigation or settlement proceeds to

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represents that the Committee reviews and approves these legal fees before passing them through to each Participating Plan.

BCBS AZ would violate ERISA. In this regard, ERISA Section 406(a)(1)(A) prohibits a plan fiduciary from causing the plan to engage in a transaction if the fiduciary knows or should know that such transaction constitutes a direct or indirect sale or exchange of any property between a plan and a party in interest. BCBS AZ, as an employer whose employees are covered by the Plan, is a party in interest with respect to the Plan under ERISA Section 3(14)(C). The Required Restorative Payments to the Plan and the Plan's potential repayment to BCBS AZ with litigation or settlement proceeds would constitute impermissible exchanges between the Plan and a party-in-interest (BCBS AZ) in violation of ERISA Section 406(a)(1)(A).

ERISA Section 406(a)(1)(B) prohibits the lending of money or other extension of credit between a plan and a party-in-interest. BCBS AZ's promise to make Required Restorative Payments to the Plan, over time, constitutes an impermissible extension of credit between the Plan and a party-in-interest in violation of ERISA Section 406(a)(1)(B).

ERISA Section 406(a)(1)(D) prohibits a plan fiduciary from causing a plan to engage in a transaction if the fiduciary knows or should know that the transaction constitutes a direct or indirect transfer to, or use by or for the benefit of, a party-in-interest, of the income or assets of the plan. The transfer of Plan assets to BCBS AZ



in connection with the Repayment would constitute an impermissible transfer of Plan assets to a party-in-interest in violation of ERISA Section 406(a)(1)(D).

#### Conditions

24. This proposed exemption contains a number of conditions that must be met. For example, the proposed exemption mandates that the Independent Fiduciary, in full accordance with its obligations of prudence and loyalty under ERISA Section 404(a)(1)(A) and (B) must:

(a) review, negotiate, and approve the terms and conditions of the Required Restorative Payments, the Repayment, and the Contribution and Assignment Agreement, before the Plan enters into such payments and the agreement;

(b) determine that the terms and conditions of the Required Restorative Payments, the Repayment, and the Contribution and Assignment Agreement are prudent, in the interest of the Plan and its participants and beneficiaries, and protective of the rights of the Plan's participants and beneficiaries;

(c) confirm that the Required Restorative Payments are fully and timely made;

(d) monitor the Claims and confirm that the Plan receives its proper share of any litigation or settlement proceeds received by the Trust in connection with the Claims;

(e) ensure that any Repayment by the Plan to BCBS AZ fully complies with the terms of this exemption and is for no more than the lesser of the total Restorative Payments actually made to the Plan by BCBS AZ or the amount the Plan received from the Claims, plus Attorney Fees;

(f) ensure that any Repayment by the Plan to BCBS AZ for legal expenses in connection with the Claims is limited to only reasonable legal expenses that were paid by BCBS AZ to unrelated third parties for representation of the Plan and its interests (as opposed to representation of BCBS AZ or the interests of any party other than the Plan) where BCBS AZ was not otherwise reimbursed from a non-Plan party;

(g) monitor the Plan's Assigned Interests on an ongoing basis to determine and confirm that any excess recovery amount from the Claims (i.e., any amount that exceeds the Required Restorative Payment Amount) is retained by the Plan;

(h) ensure that all of the conditions and definitions of this proposed exemption are met; and

(i) represent that it has not and will not enter into any agreement or instrument that violates ERISA Section 410 or Department Regulations codified at 29 CFR section 2509.75-4.<sup>27</sup>

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<sup>27</sup> ERISA Section 410 provides, in part, that "except as provided in ERISA Sections 405(b)(1) and 405(d), any provision in an agreement or instrument which purports to relieve a fiduciary from responsibility or liability for any responsibility, obligation, or duty under this part [meaning Part 4 of Title I of ERISA] shall be void as against public policy."

25. This proposed exemption also requires Gallagher to respond in writing to any information requests from the Department regarding Gallagher's activities as the Plan's Independent Fiduciary. Additionally, no later than 90 days after the resolution of the litigation, Gallagher must submit a written report to the Department demonstrating that all terms and conditions of the exemption have been met.

26. This proposed exemption requires that the Plan has not and will not release any claims, demands and/or causes of action it may have against: (a) any fiduciary of the Plan; (b) any fiduciary of the Trust; (c) BCBS AZ; and/or (d) any person or entity related to a person or entity described in (a)-(c) of this paragraph. Additionally, any Repayment by the Plan to BCBS AZ must be made in a manner designed to minimize unnecessary costs and disruption to the Plan and its investments.

27. The Plan may not make any Repayment to BCBS AZ before the date: the Plan has received from BCBS AZ the entire amount of the Restorative Payments agreed to in the Amended Contribution and Assignment Agreement; and all the Claims are settled. Furthermore, the Plan may not pay any interest to BCBS AZ in connection with its receipt of the Required Restorative Payments, nor pledge Plan assets to secure any portion of the Required Restorative Payments.

28. Pursuant to this proposed exemption, the Plan may not incur any expenses, commissions or transaction costs in connection with the Proposed Transactions. However, as noted above, under certain circumstances the Plan may reimburse BCBS AZ for reasonable legal expenses arising from the Claims that BCBS AZ paid to non-BCBS AZ-related parties for representation of the Plan and its interests (as opposed to representation of BCBS AZ or the interests of any party other than the Plan) where BCBS AZ was not otherwise reimbursed by a non-Plan party.

29. Finally, the exemptive relief provided under this proposed exemption is conditioned upon the Department's assumption that the material facts and representations set forth above in the Summary of Facts and Representation section are true and accurate at all times. In the event that a material fact or representation detailed above is untrue or inaccurate, the exemptive relief provided under this exemption will cease immediately.

#### Statutory Findings

30. ERISA Section 408(a) provides, in part, that the Department may not grant an exemption unless the Department finds that the exemption is administratively feasible, in the interest of affected plans and of their participants and beneficiaries, and protective of the

rights of such participants and beneficiaries. Each of these criteria is discussed below.

a. The Proposed Exemption Is "Administratively Feasible." The Department has tentatively determined that the proposed exemption is administratively feasible because, among other things, the Independent Fiduciary will represent the interests of the Plan for all purposes with respect to the Proposed Transactions.<sup>28</sup> In this regard, not later than 90 days after the resolution of the litigation, the Independent Fiduciary must submit a written report to the Department demonstrating that all of the requirements of this exemption have been met.

b. The Proposed Exemption Is "In the Interests of the Plan." The Department has tentatively determined that the proposed exemption is in the interest of the Plan because, among other things, the Plan's receipt of the Required Restorative Payments will substantially improve the Plan's funding status, which will enhance the Plan's ability to meet its obligations to fund benefit obligations to participants and beneficiaries and help the Plan avoid the

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<sup>28</sup> This proposed exemption would require that if the Independent Fiduciary resigns, is removed, or for any reason is unable to serve as an Independent Fiduciary, the successor Independent Fiduciary must, among other things, assume all of the duties of the outgoing Independent Fiduciary. As soon as possible, including before the appointment of a successor Independent Fiduciary, the Plan Sponsor and the Plan must notify the Department's Office of Exemption Determinations of the change in Independent Fiduciaries. The notification must contain all material information including the qualifications of the successor Independent Fiduciary.

imposition of benefit limitations imposed under Code section 436.

c. The Proposed Exemption Is "Protective of the Plan."

The Department has tentatively determined that the proposed exemption is protective of the rights of the Plan's participants and beneficiaries because, among other things, the Plan will repay BCBS AZ the lesser of the Required Restorative Payment Amount already received, or the amount the Plan receives in proceeds from the Claims, ensuring that the Proposed Transactions will result in an increase in Plan assets to: (a) an adjusted funding target attainment percentage of at least 110%; and (b) and an amount that is at least equal to or greater than 100% of the current liabilities of the Plan (less reasonable legal expenses related to the Claims paid by BCBS AZ to unrelated third parties as confirmed and approved by the Independent Fiduciary). Further, this exemption preserves any right, claim, demand and/or cause of action the Plan may have against: (a) any fiduciary of the Plan; (b) any fiduciary of the Trust; (c) BCBS AZ; and/or (d) any person or entity related to a person or entity described in (a)-(c).

Summary

31. Based on the conditions described above, the Department has tentatively determined that the relief sought by the Applicant satisfies the statutory requirements under ERISA Section 408(a) for the Department

to make findings that support its issuance of a proposed exemption.

### **PROPOSED EXEMPTION**

The Department is considering granting an exemption under the authority of ERISA Section 408(a) and Code Section 4975(c)(2) and in accordance with the procedures set forth in the Department's exemption procedure regulation.<sup>29</sup>

#### **Section I. Definitions**

(a) The term "Attorney Fees" means reasonable legal expenses paid by BCBS AZ on behalf of the Plan in connection with the Claims, if such fees are reviewed and approved by a qualified independent fiduciary who confirms that the fees were reasonably incurred and paid by BCBS AZ to unrelated third parties. For the purposes of this exemption, the Attorney Fees reimbursable to BCBS AZ do not include: (1) legal expenses paid by the Plan; and (2) legal expenses paid by BCBS AZ for representation of BCBC AZ or the interests of any party other than the Plan.

(b) The term "BCBS AZ" means Blue Cross and Blue Shield of Arizona, Inc.

(c) The term "Claims" means the legal claims against Allianz Global Investors U.S. LLC (Allianz) and Aon

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<sup>29</sup> 29 CFR part 2570, subpart B (55 FR 32836, 32847, August 10, 1990).

Investments USA Inc. (Aon), to recover certain losses incurred by the Plan in the first quarter of 2020.

(d) The term "Amended Contribution and Assignment Agreement" means the written agreement between BCBS AZ and the Plan, dated November 5, 2020, and its amendment that became effective on October 13, 2021, containing all material terms regarding BCBS AZ's agreement to make Required Restorative Payments to the Plan in return for the Plan's potential Repayment to BCBS AZ of an amount that is no more than lesser of the Required Restorative Payment Amount (as described in Section I(h)) already received or the amount of litigation proceeds the Plan receives from the Claims, plus reasonable attorney fees paid to unrelated third parties by BCBS AZ in connection with the Claims.

(e) The term "Independent Fiduciary" means Gallagher Fiduciary Advisors, LLC (Gallagher) or a successor Independent Fiduciary to the extent Gallagher or the successor Independent Fiduciary continues to serve in such capacity who:

(1) Is not an affiliate of BCBS AZ and does not hold an ownership interest in BCBS AZ or affiliates of BCBS AZ;

(2) Was not a fiduciary with respect to the Plan before its appointment to serve as the Independent Fiduciary;

(3) Has acknowledged in writing that it:



(i) is a fiduciary with respect to the Plan and has agreed not to participate in any decision regarding any transaction in which it has an interest that might affect its best judgment as a fiduciary; and

(ii) Has appropriate technical training or experience to perform the services contemplated by the exemption;

(4) Has not entered into any agreement or instrument that violates the prohibitions on exculpatory provisions in ERISA Section 410 or the Department's regulation relating to indemnification of fiduciaries;<sup>30</sup>

(5) Has not received gross income from BCBS AZ or its affiliates during any fiscal year in an amount that exceeds two percent (2%) of the Independent Fiduciary's gross income from all sources for the prior fiscal year. This provision also applies to a partnership or corporation of which the Independent Fiduciary is an officer, director, or 10 percent (10%) or more partner or shareholder, and includes as gross income amounts received as compensation for services provided as an independent fiduciary under any prohibited transaction exemption granted by the Department; and

(6) No organization or individual that is an Independent Fiduciary, and no partnership or corporation of which such organization or individual is an officer,

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<sup>30</sup> 29 CFR 2509.75-4.

director, or ten percent (10%) or more partner or shareholder, may acquire any property from, sell any property to, or borrow any funds from BCBS AZ or from affiliates of BCBS AZ while serving as an Independent Fiduciary. This prohibition will continue for six months after the party ceases to be an Independent Fiduciary and/or the Independent Fiduciary negotiates any transaction on behalf of the Plan during the period that the organization or individual serves as an Independent Fiduciary.

(f) The "Plan" means the Non-Contributory Retirement Program for Certain Employees of Blue Cross and Blue Shield of Arizona, Inc.

(g) The term "Plan Losses" means the \$302,470,379 in Plan losses the BCBSA's National Employee Benefits Committee alleges were the result of breaches of fiduciary responsibilities and breaches of contract by Allianz Global Investors U.S. LLC and/or Aon Investments USA Inc.

(h) The term "Restorative Payments" means the payments made by BCBS AZ to the Plan in connection with the Plan Losses, defined above, consisting of: (1) a first installment amount of \$60,000,000 that BCBS AZ contributed to the Plan on September 15, 2020; (2) a second installment amount of \$35,000,000 that BCBS AZ contributed to the Plan on December 28, 2020; (3) a third installment amount of \$10,000,000 that BCBS AZ contributed to the Plan on July

30, 2021; (4) a fourth installment amount of \$25,000,000 that BCBS AZ contributed to the Plan on December 21, 2021; and (5) other amounts contributed to the Plan by BCBS AZ before December 31, 2023 that are necessary for (i) the Plan to have an adjusted funding target attainment percentage of 110% after taking into account any waivers of the funding standard carryover balance by the Plan Sponsor, and (ii) the Plan's assets to be equal to or greater than 100% of the current liabilities of the Plan. The sum of (1)-(5) is the Required Restorative Payment Amount. The term "Required Restorative Payment" will not include any required minimum contributions that BCBS AZ makes to the Plan on and after October 13, 2021.

(i) The "Repayment" means the payment, if any, that the Plan will transfer to BCBS AZ following the Plan's receipt of proceeds from the Claims, where the Repayment is made following the full and complete resolution of the Claims; and in a manner that is consistent with the terms of the exemption.

## **Section II. Proposed Transactions**

If the proposed exemption is granted, the restrictions of ERISA Sections 406(a)(1)(A), (B) and (D) and the sanctions resulting from the application of Code Section 4975, by reason of Code Sections 4975(c)(1)(A), (B) and (D), shall not apply, effective September 15, 2020, to the

following transactions: BCBS AZ's transfer of Restorative Payments to the Plan; and, in return, the Plan's Repayment of an amount to BCBS AZ, which must be no more than the lesser of the Restorative Payment Amount already received or the amount of litigation proceeds the Plan received from the Claims, plus reasonable Attorney Fees, provided that the Definitions set forth in Section I and the Conditions set forth in Section III are met.

**Section III. Conditions**

(a) The Plan receives the entire Restorative Payment Amount no later than December 31, 2023;

(b) In connection with its receipt of the Required Restorative Payments, the Plan does not release any claims, demands and/or causes of action the Plan may have against the following: (1) any fiduciary of the Plan; (2) any fiduciary of the Trust; (3) BCBS AZ; and/or (4) any person or entity related to a person or entity identified in (1)-(3) of this paragraph;

(c) The Plan's Repayment to BCBS AZ is for no more than the lesser of the total Restorative Payments received by the Plan or the amount of litigation proceeds the Plan receives from the Claims. The Plan's Repayment to BCBS AZ may only occur after the Independent Fiduciary has determined that: all the conditions of the exemption are met; the Plan has received all the Restorative Payments it

is due; and the Plan has received all the litigation proceeds it is due. The Plan's Repayment to BCBS AZ must be carried out in a manner designed to minimize unnecessary costs and disruption to the Plan and its investments;

(d) A qualified independent fiduciary (the Independent Fiduciary, as further defined in Section II(e)), acting solely on behalf of the Plan in full accordance with its obligations of prudence and loyalty under ERISA Sections 404(a)(1)(A) and (B) must:

(1) Review, negotiate and approve the terms and conditions of the Restorative Payments and the Repayment and the Contribution and Assignment Agreement, all of which must be in writing, before the Plan enters into those transactions/agreement;

(2) Determine that the Restorative Payments, the Repayment, and the terms of the Contribution and Assignment Agreement, are prudent and in the interest of the Plan and its participants and beneficiaries;

(3) Confirm that the Required Restorative Payment Amount was fully and timely made;

(4) Monitor the litigation related to the Claims and confirm that the Plan receives, in a timely manner, its proper share of any litigation or settlement proceeds received by the Trust;

(5) Ensure that any Repayment by the Plan to BCBS AZ for legal expenses in connection with the Claims is

limited to only reasonable legal expenses that were paid by BCBS AZ to unrelated third parties;

(6) Ensure that all of the conditions and definitions of this proposed exemption are met;

(7) Submit a written report to the Department's Office of Exemption Determinations demonstrating and confirming that the terms and conditions of the exemption were met, within 90 days after the Repayment; and

(8) Not enter into any agreement or instrument that violates ERISA Section 410 or the Department's Regulations codified at 29 CFR Section 2509.75-4.

(f) The Plan pays no interest in connection with the Restorative Payments;

(g) The Plan does not pledge any Plan assets to secure any portion of the Restorative Payments;

(h) The Plan does not incur any expenses, commissions, or transaction costs in connection with the Proposed Transactions. However, if first approved by the Independent Fiduciary, the Plan may reimburse BCBS AZ for reasonable legal expenses paid in connection with the Claims by BCBS AZ to non-BCBS AZ-related parties. For purposes of determining the amount of Attorney Fees the Plan may reimburse to BCBS AZ under this proposal, the amount of reasonable attorney fees paid by BCBS AZ on behalf of the Plan in connection with the Claims must be reduced by the amount of legal fees received by BCBS AZ in

connection with the Claims from any non-Plan party (i.e., pursuant to a court award);

(i) The proposed transactions do not involve any risk of loss to either the Plan or the Plan's participants and beneficiaries;

(j) No party associated with this exemption has or will indemnify the Independent Fiduciary and the Independent Fiduciary will not request indemnification from any party, in whole or in part, for negligence and/or any violation of state or federal law that may be attributable to the Independent Fiduciary in performing its duties to the Plan with respect to the Proposed Transactions. In addition, no contract or instrument may purport to waive any liability under state or federal law for any such violation.

(k) If an Independent Fiduciary resigns, is removed, or for any reason is unable to serve as an Independent Fiduciary, the Independent Fiduciary must be replaced by a successor entity that: (1) meets the definition of Independent Fiduciary detailed above in Section II(e); and (2) otherwise meets all of the qualification, independence, prudence and diligence requirements set forth in this exemption. Further, any such successor Independent Fiduciary must assume all of the duties of the outgoing Independent Fiduciary. As soon as possible, including before the appointment of a successor Independent

Fiduciary, BCBS AZ must notify the Department's Office of Exemption Determinations of the change in Independent Fiduciary and such notification must contain all material information regarding the successor Independent Fiduciary, including the successor Independent Fiduciary's qualifications; and

(1) All of the material facts and representations set forth in the Summary of Facts and Representation are true and accurate at all times.

#### NOTICE TO INTERESTED PERSONS

The Applicant will give notice of the proposed exemption to all interested persons and all of the parties to the litigation described above, within fifteen calendar days after the publication of the notice of proposed exemption in the *Federal Register*. The notice will contain a copy of the notice of proposed exemption, as published in the *Federal Register*, and a supplemental statement, as required pursuant to the Department's regulations codified at 29 CFR 2570.43(a)(2). The supplemental statement will inform interested persons of their right to comment on the pending exemption. Written comments are due by [INSERT DATE THAT IS 45 DAYS FROM THE PUBLICATION OF THE NOTICE IN THE *FEDERAL REGISTER*].

All comments will be made available to the public.



**Warning:** If you submit a comment, EBSA recommends that you include your name and other contact information in the body of your comment, but DO NOT submit information that you consider to be confidential, or otherwise protected (such as a Social Security number or an unlisted phone number) or confidential business information that you do not want publicly disclosed. All comments may be posted on the Internet and can be retrieved by most Internet search engines.

*For Further Information Contact:* Mr. Frank Gonzalez of the Department, telephone (202) 693-8553. (This is not a toll-free number.)

**Blue Cross and Blue Shield of Vermont**

**Located in Berlin, Vermont**

**[Application No. D-12055]**

**Proposed Exemption**

The Department is considering granting an exemption under the authority of Section 408(a) of the Employee Retirement Income Security Act of 1974, as amended (ERISA), and Section 4975(c)(2) of the Internal Revenue Code of 1986, as amended (the Code). The proposed exemption relates to legal actions and claims (the Claims) against Allianz Global Investors U.S. LLC (Allianz) and Aon Investments USA Inc. (Aon), that arose from certain losses incurred by the Non-Contributory Retirement Program for Certain Employees of Blue Cross and Blue Shield of Vermont (the Plan) in the first quarter of 2020.<sup>31</sup>

This proposed exemption would permit the Plan sponsor, Blue Cross and Blue Shield of Vermont (BCBS VT), to make a series of payments to the Plan over a four-year period (the Restorative Payments). The Restorative Payments will

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<sup>31</sup> In proposing this exemption, the Department is not expressing an opinion regarding the merits of any Claim against Allianz and Aon, or whether the Plan's fiduciaries met their fiduciary duties with respect to Plan assets that are the subject of the Claims. Further, in proposing this exemption, the Department is not limiting any party's claim, demand and/or cause of action arising from the Plan's 2020 first quarter losses in any way. Among other things, this exemption preserves any right, claim, demand and/or cause of action the Plan may have against the following: (1) any fiduciary of the Plan; (2) any fiduciary of the Trust; (3) Blue Cross and Blue Shield of Vermont, Inc.; and/or (4) any person or entity related to a person or entity described in (1)-(3).

return the Plan to at least the Plan's funding level (126.61%) as of January 1, 2019. If the Plan receives litigation proceeds from the Claims, the Plan will transfer the lesser of the litigation proceeds amount or the Restorative Payments amount, plus reasonable attorney fees to BCBS VT.

### **SUMMARY OF FACTS AND REPRESENTATIONS<sup>32</sup>**

1. Blue Cross and Blue Shield of Vermont (BCBS VT or the Applicant) is a not-for-profit hospital and medical services corporation that issues and administers health care coverage for individuals and group health plans. BCBS VT is an independent licensee of the Blue Cross Blue Shield Association (BCBSA).

2. The Plan is an ERISA-covered qualified defined benefit pension plan that covers eligible employees of BCBS VT. As of August 31, 2020, the Plan held \$28,331,698 in total assets.

3. The Plan holds a beneficial interest in the Blue Cross and Blue Shield National Retirement Trust (the

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<sup>32</sup> The Department notes that availability of this exemption is subject to the express condition that the material facts and representations contained in application D-12055 are true and complete at all times and accurately describe all material terms of the transactions covered by the exemption. If there is any material change in a transaction covered by the exemption or in a material fact or representation described in the application, the exemption will cease to apply as of the date of such change. The Summary of Facts and Representations is based on the Applicant's representations, as well as factual representations contained in the Claims' cause of action (as described below) and does not reflect factual findings or opinions of the Department, unless indicated otherwise.

Trust). The Trust is a master trust that holds the assets of 16 defined benefit pension plans that participate in the BCBSA's National Retirement Program (the Participating Plans). Northern Trust serves as Trustee and asset custodian to the Trust and maintains separate records that reflect the net asset value of each Participating Plan. The Trust's earnings, market adjustments, and administrative expenses are allocated among the Participating Plans based on the respective Participating Plan's share of the Trust's assets. A Participating Plan's interest in the Trust's net assets is based on its share of the Trust.

4. The Committee serves as named fiduciary and administrator for each Participating Plan. The Committee is a standing committee of the BCBSA's board of directors. In 2011, the Committee invested a portion of the Trust's assets in funds managed by Allianz Global Investors U.S. LLC (Allianz), as part of a Structured Alpha Investment Strategy. These funds included: (a) AllianzGI Structured Alpha Multi-Beta Series LLC I; (b) AllianzGI Structured Alpha Emerging Markets Equity 350 LLC; and (c) AllianzGI Structured Alpha 1000 LLC (collectively, the Structured Alpha Funds).

5. The Applicant represents that the Allianz Structured Alpha strategy consisted of alpha and beta components. According to the applicant, the alpha

component was an options trading strategy that Allianz claimed would seek targeted positive return potential while maintaining structural risk protections. The beta component was intended to provide broad market exposure to a particular asset class through investments in financial products similar to an exchange-traded fund that replicates the performance of a market index, such as the S&P 500. According to the Applicant, Allianz represented that the Structured Alpha Strategy would capitalize on the return-generating features of option selling (short volatility) while simultaneously benefitting from the risk-control attributes associated with option buying (long volatility). According to the Applicant, Allianz represented further that the alpha component would include position hedging consisting of long-volatility positions designed to protect the portfolio in the event of a market crash.

6. As of December 31, 2019, the total market value of the Plan's portion of the Trust's investment in the Allianz Structured Alpha Funds was \$53,105,089, which represented 76.48% of total Plan assets.<sup>33</sup>

7. In 2009, the Committee retained Aon (then called Ennis Knupp) to provide investment advice regarding the investment of Plan assets held in the Trust. The Applicant represents that Aon provided regular investment advice

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<sup>33</sup> By proposing this exemption, the Department does not, in any way, suggest a conclusion that the Plan's fiduciaries met their ERISA Section 404 duties when they caused the Trust to invest 76.48% of the Plan's total assets in the Allianz Structured Alpha Funds.

pursuant to a written contract between it and the Committee. Pursuant to its engagement, Aon agreed to provide the following: "recommendations to [the Committee] regarding asset allocation" within the Trust; "recommendations to [the Committee] regarding the specific asset allocation and other investment guidelines" for the Trust's investment managers such as Allianz; and advice "regarding the diversification of assets" held in the Trust." The Applicant represents that Aon agreed to: conduct "active, ongoing monitoring" of Allianz to "identify any forward-looking" risks "that could impact performance;" and "inform itself" of any information necessary to discharge its duty to monitor, including information about the actual options positions Allianz had constructed.

8. The Applicant represents that when equity markets sharply declined in February and March of 2020, volatility spiked and the options positions held within the Structured Alpha Strategy were exposed to a heightened risk of loss. The Applicant represents that, unbeknownst to the Committee, and in violation of Allianz's stated investment strategy, Allianz abandoned the hedging strategy that was the supposed cornerstone of the Structured Alpha Strategy, leaving the portfolio almost entirely unhedged against a spike in market volatility. As described in the Claims, although Allianz had represented that it would buy hedges

at strike prices ranging from 10% to 25% below the market, the hedges it actually held at the end of February 2020 were as much as 60% below the market.

The Applicant represents that, as of January 31, 2020, the Trust had invested approximately \$2,916,049,486 in the Structured Alpha Strategy. Six weeks later, the Trust faced a margin call, which the Applicant states left it no choice but to liquidate the investment. The Trust was ultimately able to redeem only \$646,762,678 of its \$2,916,049,486 investment, resulting in a total loss of \$2,269,286,808.

Specifically, regarding the Plan's portion of the loss, as of December 31, 2019, the market value of the Plan's total assets was \$69,439,545. As of March 31, 2020, the market value of the Plan's total assets decreased to \$25,510,951. The Plan's total losses from the Allianz Structured Alpha Strategy were \$41,588,205, which caused the Plan to be underfunded.

9. On September 16, 2020, the Committee filed a cause of action in the United States District Court for the Southern District of New York (Case number 20-CIV-07606) against Allianz and Aon for Breach of Fiduciary Duty under ERISA Section 404, Breach of Co-Fiduciary Duty under ERISA Section 405, and violation of ERISA Section 406(b) for managing the Plan assets in its self-interest and breach of contract. It is possible that resolution of this claim and

other legal actions against Allianz and Aon in connection with the Plan's losses (the Claims) could take an extended period of time.

10. The Applicant states that rather than wait for the Claims to be resolved, BCBS VT took steps to protect Plan benefits and avoid onerous benefit restrictions under Code section 436 that could apply to the Plan as a result of a funding shortfall. Therefore, on December 21, 2020, BCBS VT and the Plan entered into a Contribution and Assignment Agreement (the Contribution and Assignment Agreement).

11. The Restorative Payments. In the Contribution and Assignment Agreement, BCBS VT agreed to make an initial \$13,000,000 lump sum payment to the Plan which was expected to restore the Plan to an AFTAP funding level of approximately 80% as of the January 1, 2021 valuation of the Plan. BCBS VT also agreed to make such additional payments to the Plan as necessary to maintain the Plan's funding level at 80% as of such date, to the extent the preliminary \$13,000,000 installment payment fails to do so.<sup>34</sup> Finally, BCBS VT stated that it intended to make subsequent installment payments to the Plan on at least an annual basis and over a four-year period to restore Plan funding to approximately the level that was reported prior

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<sup>34</sup> BCBS VT has made two Restorative Payments to the Plan: a \$13,000,000 payment remitted on December 23, 2020, and a \$3,100,000 payment remitted on September 14, 2021.



to the losses sustained within the Allianz Structured Alpha strategy.

12. Since the effective date of the Contribution and Assignment Agreement, BCBS VT has made two Restorative Payments to the Plan: a \$13,000,000 payment remitted on December 23, 2020, and a \$3,100,000 payment remitted on September 14, 2021.

13. Department's Note: This exemption, if granted, requires BCBS VT to make the Restorative Payments necessary to bring the Plan's funding percentage to at least its January 1, 2019, pre-loss funded percentage of 126.61%, by December 31, 2024. The prior restorative payments noted above in paragraph 12 together with the funding obligations noted here in paragraph 13 constitute the Required Restorative Payments under this exemption.

14. In exchange for the Restorative Payments, the Plan assigned to BCBS VT its right to retain certain litigation and/or settlement proceeds recovered from the Claims (the Assigned Interests).<sup>35</sup> Per the assignment, once the Allianz/Aon litigation is resolved and if the Plan receives litigation proceeds from the Claims, the Plan will transfer to BCBS VT a repayment (the Repayment) that does not exceed the total Restorative Payments made by BCBS VT,

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<sup>35</sup> Under the Contribution and Assignment Agreement, if the Plan receives litigation or settlement proceeds from the Claims, the proceeds would first flow to the Trust, and then each Plan's pro rata portion of the proceeds would be deposited into the individual trust funding that Plan.

plus reasonable attorney fees paid by BCBS VT on behalf of the Plan in connection with the Claims, if such fees are reviewed and approved by a qualified independent fiduciary who confirms that the fees were reasonably incurred and paid by BCBS VT to unrelated third parties (the Attorney Fees). For the purposes of this exemption, Attorney Fees reimbursable to BCBS VT do not include: (a) legal expenses paid by the Plan; and (b) legal expenses paid by BCBS VT for representation of its own interests or the interests of any party other than the Plan. For purposes of determining the amount of Attorney Fees the Plan may reimburse to BCBS VT under this exemption, the amount of reasonable attorney fees paid by BCBS VT on behalf of the Plan in connection with the Claims must be reduced by the amount of legal fees received by BCBS VT in connection with the Claims from any non-Plan party (for example, from a third party pursuant to a court award).

15. The Plan must ultimately receive at least the full value of the promised Restorative Payments, minus the Attorney Fees. The Plan may ultimately receive more than the Restorative Payment amount required under the Contribution and Assignment Agreement. If the Plan receives litigation or settlement proceeds that exceed the amount of Restorative Payments that BCBS VT has made to the Plan, the Plan's Repayment to BCBS VT will be limited to the amount of Restorative Payments actually made by BCBS

VT, plus Attorney Fees. For example, if BCBS VT made \$18,000,000 in Restorative Payments to the Plan and reasonably incurred \$100,000 in Attorney Fees, and if the Plan receives \$30,000,000 in litigation proceeds, the Plan will make a Repayment to BCBS VT totaling \$18,100,000.

16. Alternatively, if the Plan receives less litigation or settlement proceeds than the amount of Restorative Payments that BCBS VT has made to the Plan, the Plan will transfer to BCBS VT the lesser amount of litigation or settlement proceeds, plus Attorney Fees. For example, if BCBS VT made \$18,000,000 in Restorative Payments to the Plan and has reasonably incurred \$100,000 in Attorney Fees, and if the Plan receives \$10,000,000 in litigation proceeds, the Plan will make a Repayment to BCBS VT totaling \$10,100,000.

17. The Department notes that if the Plan receives any restitution that is tied to the conduct underlying the Claims but was ordered pursuant to a proceeding or directive that is external to Case number 20-CIV-07606, the disposition of such proceeds must conform to the requirements of this exemption.

18. BCBS VT retained Gallagher Fiduciary Advisors, LLC (Gallagher or the Independent Fiduciary) of New York, New York, to serve as the Plan's independent fiduciary with respect to the Required Restorative Payments and the potential repayment by the Plan of those Payments

(collectively, the Proposed Transactions). Gallagher represents that it has extensive experience in institutional investment consulting and fiduciary decision-making regarding traditional and alternative investments. Gallagher further represents that its independent fiduciary decision-making work involves acting as a fiduciary advisor or decision-maker for plans and other ERISA-regulated asset pools and that it has experience with a wide range of asset classes and litigation claims.

19. Gallagher represents that it understands its duties and responsibilities under ERISA in acting as a fiduciary on behalf of the Plan. Gallagher also acknowledges that it is authorized to take all appropriate actions to safeguard the Plan's interests, and that it will monitor the Proposed Transactions on the Plan's behalf on a continuous basis and throughout the term required by this exemption.

20. Gallagher represents that it does not have any prior relationship with any parties in interest to the Plan, including BCBS VT and any BCBS VT affiliates. Gallagher further represents the total revenues it has received from the Plan and from parties in interest to the Plan in connection with its engagement as Independent Fiduciary represents approximately 0.78% of Gallagher's total revenue.

21. Gallagher represents that no party associated with this exemption application has or will indemnify it, in whole or in part, for negligence of any kind and/or any violation of state or federal law that may be attributable to Gallagher's performance of its duties as Independent Fiduciary to the Plan with respect to the Proposed Transactions. In addition, no contract or instrument entered into by Gallagher as Independent Fiduciary may purport to waive any liability under state or federal law for any such violation.

22. On December 21, 2020, Gallagher completed an Independent Fiduciary Report (the Independent Fiduciary Report) finding that the massive losses caused by the Trust's investment in the Allianz Structured Alpha Strategy resulted in a significant reduction to the Plan's total assets and funding level. Gallagher represents that the Required Restorative Payments, which will be received by the Plan substantially in advance of a final resolution of the Claims against Allianz and Aon, should restore the Plan's funded percentage to its pre-loss funded percentage as of January 1, 2019. The restoration of the Plan's funding status will secure ongoing benefit payments to participants and beneficiaries.

Gallagher notes that the Contribution and Assignment Agreement provides that the Trust must reimburse BCBS VT only up to the Required Restorative Payment Amount

received, plus any reasonable legal expense paid to non-BCBS VT-related parties that were incurred by, or allocated to, BCBS VT as a result of the Claims.<sup>36</sup> Thus, if the Plan's ultimate recovery amount from the Claims is less than the Required Restorative Payment Amount, plus related litigation expenses that were allocated to the Plan, BCBS VT, not the Plan, will suffer the loss.

Gallagher states that the Proposed Transactions and the terms of the Contribution and Assignment Agreement were negotiated and approved by Gallagher in its role as the Plan's Independent Fiduciary. Gallagher states that it approved the Proposed Transactions only after conducting an extensive analysis of the damages suffered by the Plan as a result of the failed Allianz Structured Alpha Strategy. Gallagher represents that it conducted numerous discussions with Trust representatives and counsel, along with the Plan's representatives and counsel to ensure that the interests of the Plan's participants and beneficiaries were protected with respect to all aspects of the Proposed Transactions. Based upon its assessment, Gallagher approved the Plan's receipt of the Required Restorative Payments from BCBS VT in exchange for the Assignment.

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<sup>36</sup> Currently, legal fees and expenses associated with the Claims are being paid by most of the Participating Plan's trusts on a pro rata basis according to each Participating Plan's total invested assets held in the Master Trust's Allianz Structured Alpha Strategy before the losses were incurred in the first quarter 2020. The Applicant represents that the Committee reviews and approves these legal fees before passing them through to each Participating Plan.

## ERISA Analysis

23. Absent an exemption, the Plan's receipt of the Restorative Payments from BCBS VT in exchange for the Plan's transfer of litigation or settlement proceeds to BCBS VT would violate ERISA. In this regard, ERISA Section 406(a)(1)(A) prohibits a plan fiduciary from causing the plan to engage in a transaction if the fiduciary knows or should know that such transaction constitutes a direct or indirect sale or exchange of any property between a plan and a party in interest. BCBS VT, as an employer whose employees are covered by the Plan, is a party in interest with respect to the Plan under ERISA Section 3(14)(C). The Required Restorative Payments to the Plan and the Plan's potential repayment to BCBS VT with litigation or settlement proceeds would constitute impermissible exchanges between the Plan and a party-in-interest (BCBS VT) in violation of ERISA Section 406(a)(1)(A).

ERISA Section 406(a)(1)(B) prohibits the lending of money or other extension of credit between a plan and a party-in-interest. BCBS VT's promise to make Required Restorative Payments to the Plan, over time, constitutes an impermissible extension of credit between the Plan and a party-in-interest in violation of ERISA Section 406(a)(1)(B).

ERISA Section 406(a)(1)(D) prohibits a plan fiduciary from causing a plan to engage in a transaction if the fiduciary knows or should know that the transaction constitutes a direct or indirect transfer to, or use by or for the benefit of, a party-in-interest, of the income or assets of the plan. The transfer of Plan assets to BCBS VT in connection with the Repayment would constitute an impermissible transfer of Plan assets to a party-in-interest in violation of ERISA Section 406(a)(1)(D).

#### Conditions

24. This proposed exemption contains a number of conditions that must be met. For example, the proposed exemption mandates that the Independent Fiduciary, in full accordance with its obligations of prudence and loyalty under ERISA Section 404(a)(1)(A) and (B) must:

(a) review, negotiate, and approve the terms and conditions of the Required Restorative Payments, the Repayment, and the Contribution and Assignment Agreement, before the Plan enters into such payments and the agreement;

(b) determine that the terms and conditions of the Required Restorative Payments, the Repayment, and the Contribution and Assignment Agreement are prudent, in the interest of the Plan and its participants and beneficiaries, and protective of the rights of the Plan's participants and beneficiaries;



(c) confirm that the Required Restorative Payments are fully and timely made;

(d) monitor the Claims and confirm that the Plan receives its proper share of any litigation or settlement proceeds received by the Trust in connection with the Claims;

(e) ensure that any Repayment by the Plan to BCBS VT fully complies with the terms of this exemption and is for no more than the lesser of the total Restorative Payments actually made to the Plan by BCBS VT or the amount the Plan received from the Claims, plus Attorney Fees;

(f) ensure that any Repayment by the Plan to BCBS VT for legal expenses in connection with the Claims is limited to only reasonable legal expenses that were paid by BCBS VT to unrelated third parties for representation of the Plan and its interests (as opposed to representation of BCBS VT or the interests of any party other than the Plan) where BCBS VT was not otherwise reimbursed from a non-Plan party;

(g) monitor the Plan's Assigned Interests on an ongoing basis to determine and confirm that any excess recovery amount from the Claims (i.e., any amount that exceeds the Required Restorative Payment Amount) is retained by the Plan;

(h) ensure that all of the conditions and definitions of this proposed exemption are met; and

(i) represent that it has not and will not enter into any agreement or instrument that violates ERISA Section 410 or Department Regulations codified at 29 CFR section 2509.75-4.<sup>37</sup>

25. This proposed exemption also requires Gallagher to respond in writing to any information requests from the Department regarding Gallagher's activities as the Plan's Independent Fiduciary. Additionally, no later than 90 days after the resolution of the litigation, Gallagher must submit a written report to the Department demonstrating that all terms and conditions of the exemption have been met.

26. This proposed exemption requires that the Plan has not and will not release any claims, demands and/or causes of action it may have against: (a) any fiduciary of the Plan; (b) any fiduciary of the Trust; (c) BCBS VT; and/or (d) any person or entity related to a person or entity described in (a)-(c) of this paragraph. Additionally, any Repayment by the Plan to BCBS VT must be made in a manner designed to minimize unnecessary costs and disruption to the Plan and its investments.

27. The Plan may not make any Repayment to BCBS VT before the date: the Plan has received from BCBS VT the

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<sup>37</sup> ERISA Section 410 provides, in part, that "except as provided in ERISA Sections 405(b)(1) and 405(d), any provision in an agreement or instrument which purports to relieve a fiduciary from responsibility or liability for any responsibility, obligation, or duty under this part [meaning Part 4 of Title I of ERISA] shall be void as against public policy."

entire amount of the Restorative Payments agreed to in the Amended Contribution and Assignment Agreement; and all the Claims are settled. Furthermore, the Plan may not pay any interest to BCBS VT in connection with its receipt of the Required Restorative Payments, nor pledge Plan assets to secure any portion of the Required Restorative Payments.

28. Pursuant to this proposed exemption, the Plan may not incur any expenses, commissions or transaction costs in connection with the Proposed Transactions. However, as noted above, under certain circumstances the Plan may reimburse BCBS VT for reasonable legal expenses arising from the Claims that BCBS VT paid to non-BCBS VT-related parties for representation of the Plan and its interests (as opposed to representation of BCBS VT or the interests of any party other than the Plan) where BCBS VT was not otherwise reimbursed by a non-Plan party.

29. Finally, the exemptive relief provided under this proposed exemption is conditioned upon the Department's assumption that the material facts and representations set forth above in the Summary of Facts and Representation section are true and accurate at all times. In the event that a material fact or representation detailed above is untrue or inaccurate, the exemptive relief provided under this exemption will cease immediately.

#### Statutory Findings

30. ERISA Section 408(a) provides, in part, that the Department may not grant an exemption unless the Department finds that the exemption is administratively feasible, in the interest of affected plans and of their participants and beneficiaries, and protective of the rights of such participants and beneficiaries. Each of these criteria is discussed below.

a. The Proposed Exemption Is "Administratively Feasible." The Department has tentatively determined that the proposed exemption is administratively feasible because, among other things, the Independent Fiduciary will represent the interests of the Plan for all purposes with respect to the Proposed Transactions.<sup>38</sup> In this regard, not later than 90 days after the resolution of the litigation, the Independent Fiduciary must submit a written report to the Department demonstrating that all of the requirements of this exemption have been met.

b. The Proposed Exemption Is "In the Interests of the Plan." The Department has tentatively determined that the proposed exemption is in the interest of the Plan because, among other things, the Plan's receipt of the Required

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<sup>38</sup> This proposed exemption would require that if the Independent Fiduciary resigns, is removed, or for any reason is unable to serve as an Independent Fiduciary, the successor Independent Fiduciary must, among other things, assume all of the duties of the outgoing Independent Fiduciary. As soon as possible, including before the appointment of a successor Independent Fiduciary, the Plan Sponsor and the Plan must notify the Department's Office of Exemption Determinations of the change in Independent Fiduciaries. The notification must contain all material information including the qualifications of the successor Independent Fiduciary.

Restorative Payments will substantially improve the Plan's funding status, which will enhance the Plan's ability to meet its obligations to fund benefit obligations to participants and beneficiaries and help the Plan avoid the imposition of benefit limitations imposed under Code section 436.

c. The Proposed Exemption Is "Protective of the Plan."

The Department has tentatively determined that the proposed exemption is protective of the rights of the Plan's participants and beneficiaries because, among other things, the Plan will repay BCBS VT the lesser of the Required Restorative Payment Amount received, or the amount the Plan receives in proceeds from the Claims, ensuring that the Proposed Transactions will result in an increase in Plan assets of at least the total amount of Restorative Payments (less reasonable legal expenses related to the Claims paid by BCBS VT to unrelated third parties, as confirmed and approved by the Independent Fiduciary). Further, this exemption preserves any right, claim, demand and/or cause of action the Plan may have against: (a) any fiduciary of the Plan; (b) any fiduciary of the Trust; (c) BCBS VT; and/or (d) any person or entity related to a person or entity described in (a)-(c).

Summary

31. Based on the conditions described above, the Department has tentatively determined that the relief sought by the Applicant satisfies the statutory requirements under ERISA Section 408(a) for the Department to make findings that support its issuance of a proposed exemption.

### **PROPOSED EXEMPTION**

The Department is considering granting an exemption under the authority of ERISA Section 408(a) and Code Section 4975(c)(2) and in accordance with the procedures set forth in the Department's exemption procedure regulation.<sup>39</sup>

#### **Section I. Definitions**

(a) The term "Attorney Fees" means reasonable legal expenses paid by BCBS VT on behalf of the Plan in connection with the Claims, if such fees are reviewed and approved by a qualified independent fiduciary who confirms that the fees were reasonably incurred and paid by BCBS VT to unrelated third parties. For the purposes of this exemption, the Attorney Fees reimbursable to BCBS VT do not include: (1) legal expenses paid by the Plan; and (2) legal expenses paid by BCBS VT for representation of BCBS VT or the interests of any party other than the Plan.

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<sup>39</sup> 29 CFR part 2570, subpart B (55 FR 32836, 32847, August 10, 1990).

(b) The term "BCBS VT" means Blue Cross and Blue Shield of Vermont.

(c) The term "Claims" means the legal claims against Allianz Global Investors U.S. LLC (Allianz) and Aon Investments USA Inc. (Aon), to recover certain losses incurred by the Plan in the first quarter of 2020.

(d) The term "Contribution and Assignment Agreement" means the written agreement between BCBS VT and the Plan, dated December 21, 2020, containing all material terms regarding BCBS VT's agreement to make Restorative Payments (as described in Section I(h)) to the Plan in return for the Plan's potential Repayment to BCBS VT of an amount that is no more than the lesser of the total Restorative Payments or the amount of litigation proceeds the Plan receives from the Claims, plus reasonable Attorney Fees paid to unrelated third parties by BCBS VT in connection with the Claims.

(e) The term "Independent Fiduciary" means Gallagher Fiduciary Advisors, LLC (Gallagher) or a successor Independent Fiduciary to the extent Gallagher or the successor Independent Fiduciary continues to serve in such capacity who:

(1) Is not an affiliate of BCBS VT and does not hold an ownership interest in BCBS VT or affiliates of BCBS VT;

(2) Was not a fiduciary with respect to the Plan before its appointment to serve as the Independent Fiduciary;

(3) Has acknowledged in writing that it:

(i) is a fiduciary with respect to the Plan and has agreed not to participate in any decision regarding any transaction in which it has an interest that might affect its best judgment as a fiduciary; and

(ii) Has appropriate technical training or experience to perform the services contemplated by the exemption;

(4) Has not entered into any agreement or instrument that violates the prohibitions on exculpatory provisions in ERISA Section 410 or the Department's regulation relating to indemnification of fiduciaries;<sup>40</sup>

(5) Has not received gross income from BCBS VT or its affiliates during any fiscal year in an amount that exceeds two percent (2%) of the Independent Fiduciary's gross income from all sources for the prior fiscal year. This provision also applies to a partnership or corporation of which the Independent Fiduciary is an officer, director, or 10 percent (10%) or more partner or shareholder, and includes as gross income amounts received as compensation for services provided as an independent fiduciary under any

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<sup>40</sup> 29 CFR 2509.75-4.



prohibited transaction exemption granted by the Department;  
and

(6) No organization or individual that is an Independent Fiduciary, and no partnership or corporation of which such organization or individual is an officer, director, or ten percent (10%) or more partner or shareholder, may acquire any property from, sell any property to, or borrow any funds from BCBS VT or from affiliates of BCBS VT while serving as an Independent Fiduciary. This prohibition will continue for six months after the party ceases to be an Independent Fiduciary and/or the Independent Fiduciary negotiates any transaction on behalf of the Plan during the period that the organization or individual serves as an Independent Fiduciary.

(f) The "Plan" means the Non-Contributory Retirement Program for Certain Employees of Blue Cross and Blue Shield of Vermont.

(g) The term "Plan Losses" means the \$41,588,205 in Plan losses the BCBSA's National Employee Benefits Committee alleges were the result of breaches of fiduciary responsibilities and breaches of contract by Allianz Global Investors U.S. LLC and/or Aon Investments USA Inc.

(h) The term "Restorative Payments" means the payments made by BCBS VT to the Plan in connection with the Plan Losses, including: (1) the past payment of \$13,000,000 made

on December 23, 2020, (2) the past payment of \$3,100,000 made on September 14, 2021, and (3) amounts necessary to restore the Plan to its funding level of 126.91% before December 31, 2024. The sum of (1)-(3) is the Required Restorative Payment Amount.

(i) The "Repayment" means the payment, if any, that the Plan will transfer to BCBS VT following the Plan's receipt of proceeds from the Claims, where the Repayment is made following the full and complete resolution of the Claims; and in a manner that is consistent with the terms of the exemption.

## **Section II. Proposed Transactions**

If the proposed exemption is granted, the restrictions of ERISA Sections 406(a)(1)(A), (B) and (D) and the sanctions resulting from the application of Code Section 4975, by reason of Code Sections 4975(c)(1)(A), (B) and (D), shall not apply, effective December 21, 2020, to the following transactions: BCBS VT's transfer of Restorative Payments to the Plan; and, in return, the Plan's Repayment of an amount to BCBS VT, which must be no more than the lesser of the Restorative Payment Amount or the amount of litigation proceeds the Plan received from the Claims, plus reasonable Attorney Fees, provided that the Definitions set forth in Section I and the Conditions set forth in Section III are met.

### **Section III. Conditions**

(a) The Plan receives the entire Restorative Payment Amount no later than December 31, 2024;

(b) In connection with its receipt of the Required Restorative Payments, the Plan does not release any claims, demands and/or causes of action the Plan may have against the following: (1) any fiduciary of the Plan; (2) any fiduciary of the Trust; (3) BCBS VT; and/or (4) any person or entity related to a person or entity identified in (1)-(3) of this paragraph;

(c) The Plan's Repayment to BCBS VT is for no more than the lesser of the total Restorative Payments received by the Plan or the amount of litigation proceeds the Plan receives from the Claims. The Plan's Repayment to BCBS VT may only occur after the Independent Fiduciary has determined that: all the conditions of the exemption are met; the Plan has received all the Restorative Payments it is due; and the Plan has received all the litigation proceeds it is due. The Plan's Repayment to BCBS VT must be carried out in a manner designed to minimize unnecessary costs and disruption to the Plan and its investments;

(d) A qualified independent fiduciary (the Independent Fiduciary, as further defined in Section II(e)), acting solely on behalf of the Plan in full accordance with its

obligations of prudence and loyalty under ERISA Sections 404(a)(1)(A) and (B) must:

(1) Review, negotiate and approve the terms and conditions of the Restorative Payments and the Repayment and the Contribution and Assignment Agreement, all of which must be in writing, before the Plan enters into those transactions/agreement;

(2) Determine that the Restorative Payments, the Repayment, and the terms of the Contribution and Assignment Agreement, are prudent and in the interest of the Plan and its participants and beneficiaries;

(3) Confirm that the Required Restorative Payment Amount was fully and timely made;

(4) Monitor the litigation related to the Claims and confirm that the Plan receives, in a timely manner, its proper share of any litigation or settlement proceeds received by the Trust;

(5) Ensure that any Repayment by the Plan to BCBS VT for legal expenses in connection with the Claims is limited to only reasonable legal expenses that were paid by BCBS VT to unrelated third parties;

(6) Ensure that all of the conditions and definitions of this proposed exemption are met;

(7) Submit a written report to the Department's Office of Exemption Determinations demonstrating and

confirming that the terms and conditions of the exemption were met, within 90 days after the Repayment; and

(8) Not enter into any agreement or instrument that violates ERISA Section 410 or the Department's Regulations codified at 29 CFR Section 2509.75-4.

(f) The Plan pays no interest in connection with the Restorative Payments;

(g) The Plan does not pledge any Plan assets to secure any portion of the Restorative Payments;

(h) The Plan does not incur any expenses, commissions, or transaction costs in connection with the Proposed Transactions. However, if first approved by the Independent Fiduciary, the Plan may reimburse BCBS VT for reasonable legal expenses paid in connection with the Claims by BCBS VT to non-BCBS VT-related parties. For purposes of determining the amount of Attorney Fees the Plan may reimburse to BCBS VT under this proposal, the amount of reasonable attorney fees paid by BCBS VT on behalf of the Plan in connection with the Claims must be reduced by the amount of legal fees received by BCBS VT in connection with the Claims from any non-Plan party (i.e., pursuant to a court award);

(i) The proposed transactions do not involve any risk of loss to either the Plan or the Plan's participants and beneficiaries;

(j) No party associated with this exemption has or will indemnify the Independent Fiduciary and the Independent Fiduciary will not request indemnification from any party, in whole or in part, for negligence and/or any violation of state or federal law that may be attributable to the Independent Fiduciary in performing its duties to the Plan with respect to the Proposed Transactions. In addition, no contract or instrument may purport to waive any liability under state or federal law for any such violation.

(k) If an Independent Fiduciary resigns, is removed, or for any reason is unable to serve as an Independent Fiduciary, the Independent Fiduciary must be replaced by a successor entity that: (1) meets the definition of Independent Fiduciary detailed above in Section II(e); and (2) otherwise meets all of the qualification, independence, prudence and diligence requirements set forth in this exemption. Further, any such successor Independent Fiduciary must assume all of the duties of the outgoing Independent Fiduciary. As soon as possible, including before the appointment of a successor Independent Fiduciary, BCBS VT must notify the Department's Office of Exemption Determinations of the change in Independent Fiduciary and such notification must contain all material information regarding the successor Independent Fiduciary,

including the successor Independent Fiduciary's qualifications; and

(1) All of the material facts and representations set forth in the Summary of Facts and Representation are true and accurate at all times.

#### NOTICE TO INTERESTED PERSONS

The Applicant will give notice of the proposed exemption to all interested persons and all of the parties to the litigation described above, within fifteen calendar days after the publication of the notice of proposed exemption in the *Federal Register*. The notice will contain a copy of the notice of proposed exemption, as published in the *Federal Register*, and a supplemental statement, as required pursuant to the Department's regulations codified at 29 CFR 2570.43(a)(2). The supplemental statement will inform interested persons of their right to comment on the pending exemption. Written comments are due by [INSERT DATE THAT IS 45 DAYS FROM THE PUBLICATION OF THE NOTICE IN THE *FEDERAL REGISTER*].

All comments will be made available to the public.

**Warning:** If you submit a comment, EBSA recommends that you include your name and other contact information in the body of your comment, but DO NOT submit information that you consider to be confidential, or otherwise protected (such as a Social Security number or an unlisted phone number) or

confidential business information that you do not want publicly disclosed. All comments may be posted on the Internet and can be retrieved by most Internet search engines.

*For Further Information Contact:* Mr. Nicholas Schroth of the Department, telephone (202) 693-8571. (This is not a toll-free number.)

**Hawaii Medical Service Association**

**Located in Honolulu, Hawaii**

**[Application No. D-12038]**

### **Proposed Exemption**

The Department is considering granting an exemption under the authority of Section 408(a) of the Employee Retirement Income Security Act of 1974, as amended (ERISA), and Section 4975(c)(2) of the Internal Revenue Code of 1986, as amended (the Code). The proposed exemption relates to legal actions and claims (the Claims) against Allianz Global Investors U.S. LLC (Allianz) and Aon Investments USA Inc. (Aon), that arose from certain losses incurred by the Non-Contributory Retirement Program for Certain Employees of Hawaii Medical Service Association (the Plan) in the first quarter of 2020.<sup>41</sup>

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<sup>41</sup> In proposing this exemption, the Department is not expressing an opinion regarding the merits of any Claim against Allianz and Aon, or whether the Plan's fiduciaries met their fiduciary duties with respect



This proposed exemption would permit the past payment of \$50,000,000 by Hawaii Medical Service Association (HMSA), the Plan sponsor, to the Plan (the Restorative Payment). If the Plan receives litigation proceeds from the Claims, the Plan will transfer the lesser of the litigation proceeds amount or the Restorative Payment amount, plus reasonable attorney fees to HMSA.

#### **SUMMARY OF FACTS AND REPRESENTATIONS<sup>42</sup>**

1. HMSA is a not-for-profit company that provides health insurance products and services. HMSA is an independent licensee of the Blue Cross Blue Shield Association (BCBSA).

2. The Plan is an ERISA-covered qualified defined benefit pension plan that covers eligible employees of HMSA and employees of affiliated employers. On December 31,

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to Plan assets that are the subject of the Claims. Further, in proposing this exemption, the Department is not limiting any party's claim, demand and/or cause of action arising from the Plan's 2020 first quarter losses in any way. Among other things, this exemption preserves any right, claim, demand and/or cause of action the Plan may have against the following: (1) any fiduciary of the Plan; (2) any fiduciary of the Trust; (3) Hawaii Medical Service Association; and/or (4) any person or entity related to a person or entity described in (1)-(3).

<sup>42</sup> The Department notes that availability of this exemption is subject to the express condition that the material facts and representations contained in application D-12038 are true and complete at all times and accurately describe all material terms of the transactions covered by the exemption. If there is any material change in a transaction covered by the exemption or in a material fact or representation described in the application, the exemption will cease to apply as of the date of such change. The Summary of Facts and Representations is based on the Applicant's representations, as well as factual representations contained in the Claims' cause of action (as described below) and does not reflect factual findings or opinions of the Department, unless indicated otherwise.

2014, the Plan was closed to new entrants. In August 2020, the Sponsor elected to freeze Plan benefits for all participants effective December 31, 2024. As of December 31, 2020, the Plan covered 1,638 participants and held \$167,536,184 in total assets.

3. Up until 2020, the Plan held a beneficial interest in the Blue Cross and Blue Shield National Retirement Trust (the Trust).<sup>43</sup> The Trust is a master trust that holds the assets of 16 defined benefit pension plans that participate in the BCBSA's National Retirement Program (the Participating Plans). Northern Trust serves as Trustee and asset custodian to the Trust and maintains separate records that reflect the net asset value of each Participating Plan. The Trust's earnings, market adjustments, and administrative expenses are allocated among the Participating Plans based on the respective Participating Plan's share of the Trust's assets. A Participating Plan's interest in the Trust's net assets is based on its share of the Trust.

4. The Committee serves as named fiduciary and administrator for each Participating Plan. The Committee is a standing committee of the BCBSA's board of directors. In 2011, the Committee invested a portion of the Trust's assets in funds managed by Allianz Global Investors U.S.

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<sup>43</sup> The Plan withdrew substantially all of its assets from the Trust in advance of the Trust's August 31, 2020 valuation date.

LLC (Allianz), as part of a Structured Alpha Investment Strategy. These funds included: (a) AllianzGI Structured Alpha Multi-Beta Series LLC I; (b) AllianzGI Structured Alpha Emerging Markets Equity 350 LLC; and (c) AllianzGI Structured Alpha 1000 LLC (collectively, the Structured Alpha Funds).

5. The Applicant represents that the Allianz Structured Alpha strategy consisted of alpha and beta components. According to the applicant, the alpha component was an options trading strategy that Allianz claimed would seek targeted positive return potential while maintaining structural risk protections. The beta component was intended to provide broad market exposure to a particular asset class through investments in financial products similar to an exchange-traded fund that replicates the performance of a market index, such as the S&P 500. According to the Applicant, Allianz represented that the Structured Alpha Strategy would capitalize on the return-generating features of option selling (short volatility) while simultaneously benefitting from the risk-control attributes associated with option buying (long volatility). According to the Applicant, Allianz represented further that the alpha component would include position hedging consisting of long-volatility positions designed to protect the portfolio in the event of a market crash.

6. As of December 31, 2019, the total market value of the Plan's portion of the Trust's investment in the Allianz Structured Alpha Funds was \$229,799,688, which represented 86.11% of total Plan assets.<sup>44</sup>

7. In 2009, the Committee retained Aon (then called Ennis Knupp) to provide investment advice regarding the investment of Plan assets held in the Trust. The Applicant represents that Aon provided regular investment advice pursuant to a written contract between it and the Committee. Pursuant to its engagement, Aon agreed to provide the following: "recommendations to [the Committee] regarding asset allocation" within the Trust; "recommendations to [the Committee] regarding the specific asset allocation and other investment guidelines" for the Trust's investment managers such as Allianz; and advice "regarding the diversification of assets" held in the Trust." The Applicant represents that Aon agreed to: conduct "active, ongoing monitoring" of Allianz to "identify any forward-looking" risks "that could impact performance;" and "inform itself" of any information necessary to discharge its duty to monitor, including information about the actual options positions Allianz had constructed.

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<sup>44</sup> By proposing this exemption, the Department does not, in any way, suggest a conclusion that the Plan's fiduciaries met their ERISA Section 404 duties when they caused the Trust to invest 86.11% of the Plan's total assets in the Allianz Structured Alpha Funds.

8. The Applicant represents that when equity markets sharply declined in February and March of 2020, volatility spiked and the options positions held within the Structured Alpha Strategy were exposed to a heightened risk of loss. The Applicant represents that, unbeknownst to the Committee, and in violation of Allianz's stated investment strategy, Allianz abandoned the hedging strategy that was the supposed cornerstone of the Structured Alpha Strategy, leaving the portfolio almost entirely unhedged against a spike in market volatility. As described in the Claims, although Allianz had represented that it would buy hedges at strike prices ranging from 10% to 25% below the market, the hedges it actually held at the end of February 2020 were as much as 60% below the market.

The Applicant represents that, as of January 31, 2020, the Trust had invested approximately \$2,916,049,486 in the Structured Alpha Strategy. Six weeks later, the Trust faced a margin call, which the Applicant states left it no choice but to liquidate the investment. The Trust was ultimately able to redeem only \$646,762,678 of its \$2,916,049,486 investment, resulting in a total loss of \$2,269,286,808.

Specifically, regarding the Plan's portion of the loss, as of December 31, 2019, the market value of the Plan was \$266,849,059. As of March 31, 2020, the market value of the Plan's total assets decreased to \$90,420,304. The

Applicant represents that the Plan's total losses from the Allianz Structured Alpha Strategy were \$187,271,581, which caused the Plan to be underfunded.

9. On September 16, 2020, the Committee filed a cause of action in the United States District Court for the Southern District of New York (Case number 20-CIV-07606) against Allianz and Aon for Breach of Fiduciary Duty under ERISA Section 404, Breach of Co-Fiduciary Duty under ERISA Section 405, and violation of ERISA Section 406(b) for managing the Plan assets in its self-interest and breach of contract. It is possible that resolution of this claim and other legal actions against Allianz and Aon in connection with the Plan's losses (the Claims) could take an extended period of time.

10. The Applicant states that rather than wait for the Claims to be resolved, HMSA took steps to protect Plan benefits and avoid onerous benefit restrictions under Code section 436 that could apply to the Plan as a result of a funding shortfall. Therefore, on November 3, 2020, HMSA and the Plan entered into a Contribution and Assignment Agreement (the Contribution and Assignment Agreement) whereby HMSA agreed to make a \$50,000,000 Restorative Payment to the Plan. Subsequently, on December 18, 2020, HMSA made a \$50,000,000 Restorative Payment to the Plan. This \$50,000,000 payment is the Required Restorative Payment Amount under this exemption.

11. In exchange for the Restorative Payment, the Plan assigned to HMSA its right to retain certain litigation and/or settlement proceeds recovered from the Claims (the Assigned Interests).<sup>45</sup> Per the assignment, once the Allianz/Aon litigation is resolved and if the Plan receives litigation proceeds from the Claims, the Plan will transfer to HMSA a repayment (the Repayment) that does not exceed the total Restorative Payment made by HMSA as of that date, plus reasonable attorney fees paid by HMSA on behalf of the Plan in connection with the Claims, if such fees are reviewed and approved by a qualified independent fiduciary who confirms that the fees were reasonably incurred and paid by HMSA to unrelated third parties (the Attorney Fees).

For the purposes of this exemption, Attorney Fees reimbursable to HMSA do not include: (a) legal expenses paid by the Plan; and (b) legal expenses paid by HMSA for representation of its own interests or the interests of any party other than the Plan. For purposes of determining the amount of Attorney Fees the Plan may reimburse to HMSA under this exemption, the amount of reasonable attorney fees paid by HMSA on behalf of the Plan in connection with the Claims must be reduced by the amount of legal fees

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<sup>45</sup> Under the Contribution and Assignment Agreement, if the Plan receives litigation or settlement proceeds from the Claims, the proceeds would first flow to the Trust, and then each Plan's pro rata portion of the proceeds would be deposited into the individual trust funding that Plan.

received by HMSA in connection with the Claims from any non-Plan party (for example, from a third party pursuant to a court award).

12. The Plan must ultimately receive at least the full value of the promised Restorative Payment, minus the Attorney Fees. The Plan may ultimately receive more than the Restorative Payment amount required under the Contribution and Assignment Agreement. If the Plan receives litigation or settlement proceeds that exceed the \$50,000,000 Restorative Payment that HMSA made to the Plan, the Plan's Repayment to HMSA will be limited to \$50,000,000 plus Attorney Fees. For example, if the Plan receives \$80,000,000 in litigation proceeds and HMSA has reasonably incurred \$100,000 in Attorney Fees, the Plan will make a Repayment to HMSA totaling \$50,100,000.

13. Alternatively, if the Plan receives less litigation or settlement proceeds than the \$50,000,000 Restorative Payment that HMSA made to the Plan, the Plan will transfer to HMSA the lesser amount of litigation or settlement proceeds, plus Attorney Fees. For example, if the Plan receives \$30,000,000 in litigation proceeds and HMSA has reasonably incurred \$100,000 in Attorney Fees, the Plan will make a Repayment to HMSA totaling \$30,100,000.

14. The Department notes that if the Plan receives any restitution that is tied to the conduct underlying the Claims but was ordered pursuant to a proceeding or



directive that is external to Case number 20-CIV-07606, the disposition of such proceeds must conform to the requirements of this exemption.

15. HMSA retained Gallagher Fiduciary Advisors, LLC (Gallagher or the Independent Fiduciary) of New York, New York, to serve as the Plan's independent fiduciary with respect to the Required Restorative Payment and the potential repayment by the Plan of those Payments (collectively, the Proposed Transactions). Gallagher represents that it has extensive experience in institutional investment consulting and fiduciary decision-making regarding traditional and alternative investments. Gallagher further represents that its independent fiduciary decision-making work involves acting as a fiduciary advisor or decision-maker for plans and other ERISA-regulated asset pools and that it has experience with a wide range of asset classes and litigation claims.

16. Gallagher represents that it understands its duties and responsibilities under ERISA in acting as a fiduciary on behalf of the Plan. Gallagher also acknowledges that it is authorized to take all appropriate actions to safeguard the Plan's interests, and that it will monitor the Proposed Transactions on the Plan's behalf on a continuous basis and throughout the term required by this exemption.

17. Gallagher represents that it does not have any prior relationship with any parties in interest to the Plan, including HMSA and any HMSA affiliates. Gallagher further represents the total revenues it has received from the Plan and from parties in interest to the Plan in connection with its engagement as Independent Fiduciary represents approximately 0.78% of Gallagher's total revenue.

18. Gallagher represents that no party associated with this exemption application has or will indemnify it, in whole or in part, for negligence of any kind and/or any violation of state or federal law that may be attributable to Gallagher's performance of its duties as Independent Fiduciary to the Plan with respect to the Proposed Transactions. In addition, no contract or instrument entered into by Gallagher as Independent Fiduciary may purport to waive any liability under state or federal law for any such violation.

19. On March 18, 2021, Gallagher completed an Independent Fiduciary Report (the Independent Fiduciary Report) finding that the massive losses caused by the Trust's investment in the Allianz Structured Alpha Strategy resulted in a significant reduction to the Plan's total assets and funding level. Gallagher represents that the Required Restorative Payment, which will be received by the Plan substantially in advance of a final resolution of the

Claims against Allianz and Aon, should restore the Plan's funded percentage to its pre-loss funded percentage as of January 1, 2019. The restoration of the Plan's funding status will secure ongoing benefit payments to participants and beneficiaries.

Gallagher notes that the Contribution and Assignment Agreement provides that the Trust must reimburse HMSA only up to the Required Restorative Payment Amount, plus any reasonable legal expense paid to non-HMSA-related parties that were incurred by, or allocated to, HMSA as a result of the Claims.<sup>46</sup> Thus, if the Plan's ultimate recovery amount from the Claims is less than the Required Restorative Payment Amount, plus related litigation expenses that were allocated to the Plan, HMSA, not the Plan, will suffer the loss.

Gallagher states that the Proposed Transactions and the terms of the Contribution and Assignment Agreement were negotiated and approved by Gallagher in its role as the Plan's Independent Fiduciary. Gallagher states that it approved the Proposed Transactions only after conducting an extensive analysis of the damages suffered by the Plan as a result of the failed Allianz Structured Alpha Strategy.

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<sup>46</sup> Currently, legal fees and expenses associated with the Claims are being paid by most of the Participating Plan's trusts on a pro rata basis according to each Participating Plan's total invested assets held in the Master Trust's Allianz Structured Alpha Strategy before the losses were incurred in the first quarter 2020. The Applicant represents that the Committee reviews and approves these legal fees before passing them through to each Participating Plan.

Gallagher represents that it conducted numerous discussions with Trust representatives and counsel, along with the Plan's representatives and counsel to ensure that the interests of the Plan's participants and beneficiaries were protected with respect to all aspects of the Proposed Transactions. Based upon its assessment, Gallagher approved the Plan's receipt of the Required Restorative Payment from HMSA in exchange for the Assignment.

#### ERISA Analysis

20. Absent an exemption, the Plan's receipt of the Restorative Payment from HMSA in exchange for the Plan's transfer of litigation or settlement proceeds to HMSA would violate ERISA. In this regard, ERISA Section 406(a)(1)(A) prohibits a plan fiduciary from causing the plan to engage in a transaction if the fiduciary knows or should know that such transaction constitutes a direct or indirect sale or exchange of any property between a plan and a party in interest. HMSA, as an employer whose employees are covered by the Plan, is a party in interest with respect to the Plan under ERISA Section 3(14)(C). The Required Restorative Payment to the Plan and the Plan's potential repayment to HMSA with litigation or settlement proceeds would constitute impermissible exchanges between the Plan and a party-in-interest (HMSA) in violation of ERISA Section 406(a)(1)(A).

ERISA Section 406(a)(1)(D) prohibits a plan fiduciary from causing a plan to engage in a transaction if the fiduciary knows or should know that the transaction constitutes a direct or indirect transfer to, or use by or for the benefit of, a party-in-interest, of the income or assets of the plan. The transfer of Plan assets to HMSA in connection with the Repayment would constitute an impermissible transfer of Plan assets to a party-in-interest in violation of ERISA Section 406(a)(1)(D).

#### Conditions

21. This proposed exemption contains a number of conditions that must be met. For example, the proposed exemption mandates that the Independent Fiduciary, in full accordance with its obligations of prudence and loyalty under ERISA Section 404(a)(1)(A) and (B) must:

(a) review, negotiate, and approve the terms and conditions of the Required Restorative Payment, the Repayment, and the Contribution and Assignment Agreement, before the Plan enters into such payments and the agreement;

(b) determine that the terms and conditions of the Required Restorative Payment, the Repayment, and the Contribution and Assignment Agreement are prudent, in the interest of the Plan and its participants and beneficiaries, and protective of the rights of the Plan's participants and beneficiaries;

(c) confirm that the Required Restorative Payment was fully and timely made;

(d) monitor the Claims and confirm that the Plan receives its proper share of any litigation or settlement proceeds received by the Trust in connection with the Claims;

(e) ensure that any Repayment by the Plan to HMSA fully complies with the terms of this exemption and is for no more than the lesser of the total Restorative Payment actually made to the Plan by HMSA or the amount the Plan received from the Claims, plus Attorney Fees;

(f) ensure that any Repayment by the Plan to HMSA for legal expenses in connection with the Claims is limited to only reasonable legal expenses that were paid by HMSA to unrelated third parties for representation of the Plan and its interests (as opposed to representation of HMSA or the interests of any party other than the Plan) where HMSA was not otherwise reimbursed from a non-Plan party;

(g) monitor the Plan's Assigned Interests on an ongoing basis to determine and confirm that any excess recovery amount from the Claims (i.e., any amount that exceeds the Required Restorative Payment Amount) is retained by the Plan;

(h) ensure that all of the conditions and definitions of this proposed exemption are met; and

(i) represent that it has not and will not enter into any agreement or instrument that violates ERISA Section 410 or Department Regulations codified at 29 CFR section 2509.75-4.<sup>47</sup>

22. This proposed exemption also requires Gallagher to respond in writing to any information requests from the Department regarding Gallagher's activities as the Plan's Independent Fiduciary. Additionally, no later than 90 days after the resolution of the litigation, Gallagher must submit a written report to the Department demonstrating that all terms and conditions of the exemption have been met.

23. This proposed exemption requires that the Plan has not and will not release any claims, demands and/or causes of action it may have against: (a) any fiduciary of the Plan; (b) any fiduciary of the Trust; (c) HMSA; and/or (d) any person or entity related to a person or entity described in (a)-(c) of this paragraph. Additionally, any Repayment by the Plan to HMSA must be made in a manner designed to minimize unnecessary costs and disruption to the Plan and its investments.

24. The Plan may not make any Repayment to HMSA before the date: the Plan has received from HMSA the entire

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<sup>47</sup> ERISA Section 410 provides, in part, that "except as provided in ERISA Sections 405(b)(1) and 405(d), any provision in an agreement or instrument which purports to relieve a fiduciary from responsibility or liability for any responsibility, obligation, or duty under this part [meaning Part 4 of Title I of ERISA] shall be void as against public policy."

amount of the Restorative Payment agreed to in the Contribution and Assignment Agreement; and all the Claims are settled. Furthermore, the Plan may not pay any interest to HMSA in connection with its receipt of the Required Restorative Payment, nor pledge Plan assets to secure any portion of the Required Restorative Payment.

25. Pursuant to this proposed exemption, the Plan may not incur any expenses, commissions or transaction costs in connection with the Proposed Transactions. However, as noted above, under certain circumstances the Plan may reimburse HMSA for reasonable legal expenses arising from the Claims that HMSA paid to non-HMSA-related parties for representation of the Plan and its interests (as opposed to representation of HMSA or the interests of any party other than the Plan) where HMSA was not otherwise reimbursed by a non-Plan party.

26. Finally, the exemptive relief provided under this proposed exemption is conditioned upon the Department's assumption that the material facts and representations set forth above in the Summary of Facts and Representation section are true and accurate at all times. In the event that a material fact or representation detailed above is untrue or inaccurate, the exemptive relief provided under this exemption will cease immediately.

#### Statutory Findings



27. ERISA Section 408(a) provides, in part, that the Department may not grant an exemption unless the Department finds that the exemption is administratively feasible, in the interest of affected plans and of their participants and beneficiaries, and protective of the rights of such participants and beneficiaries. Each of these criteria is discussed below.

a. The Proposed Exemption Is "Administratively Feasible." The Department has tentatively determined that the proposed exemption is administratively feasible because, among other things, the Independent Fiduciary will represent the interests of the Plan for all purposes with respect to the Proposed Transactions.<sup>48</sup> In this regard, not later than 90 days after the resolution of the litigation, the Independent Fiduciary must submit a written report to the Department demonstrating that all of the requirements of this exemption have been met.

b. The Proposed Exemption Is "In the Interests of the Plan." The Department has tentatively determined that the proposed exemption is in the interest of the Plan because, among other things, the Plan's receipt of the Required

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<sup>48</sup> This proposed exemption would require that if the Independent Fiduciary resigns, is removed, or for any reason is unable to serve as an Independent Fiduciary, the successor Independent Fiduciary must, among other things, assume all of the duties of the outgoing Independent Fiduciary. As soon as possible, including before the appointment of a successor Independent Fiduciary, the Plan Sponsor and the Plan must notify the Department's Office of Exemption Determinations of the change in Independent Fiduciaries. The notification must contain all material information including the qualifications of the successor Independent Fiduciary.

Restorative Payment will substantially improve the Plan's funding status, which will enhance the Plan's ability to meet its obligations to fund benefit obligations to participants and beneficiaries and help the Plan avoid the imposition of benefit limitations imposed under Code section 436.

c. The Proposed Exemption Is "Protective of the Plan."

The Department has tentatively determined that the proposed exemption is protective of the rights of the Plan's participants and beneficiaries because, among other things, the Plan will repay HMSA the lesser of the Required Restorative Payment Amount, or the amount the Plan receives in proceeds from the Claims, ensuring that the Proposed Transactions will result in an increase in Plan assets of at least the total amount of Restorative Payment (less reasonable legal expenses related to the Claims paid by HMSA to unrelated third parties, as confirmed and approved by the Independent Fiduciary). Further, this exemption preserves any right, claim, demand and/or cause of action the Plan may have against: (a) any fiduciary of the Plan; (b) any fiduciary of the Trust; (c) HMSA; and/or (d) any person or entity related to a person or entity described in (a)-(c).

Summary

28. Based on the conditions described above, the Department has tentatively determined that the relief sought by the Applicant satisfies the statutory

requirements under ERISA Section 408(a) for the Department to make findings that support its issuance of a proposed exemption.

### **PROPOSED EXEMPTION**

The Department is considering granting an exemption under the authority of ERISA Section 408(a) and Code Section 4975(c)(2) and in accordance with the procedures set forth in the Department's exemption procedure regulation.<sup>49</sup>

#### **Section I. Definitions**

(a) The term "Attorney Fees" means reasonable legal expenses paid by HMSA on behalf of the Plan in connection with the Claims, if such fees are reviewed and approved by a qualified independent fiduciary who confirms that the fees were reasonably incurred and paid by HMSA to unrelated third parties. For the purposes of this exemption, the Attorney Fees reimbursable to HMSA do not include: (1) legal expenses paid by the Plan; and (2) legal expenses paid by HMSA for representation of HMSA or the interests of any party other than the Plan.

(b) The term "Claims" means the legal claims against Allianz Global Investors U.S. LLC (Allianz) and Aon

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<sup>49</sup> 29 CFR part 2570, subpart B (55 FR 32836, 32847, August 10, 1990).

Investments USA Inc. (Aon), to recover certain losses incurred by the Plan in the first quarter of 2020.

(c) The term "Contribution and Assignment Agreement" means the written agreement between HMSA and the Plan, dated November 3, 2020, containing all material terms regarding HMSA's agreement to make a \$50,000,000 payment to the Plan in return for the Plan's potential Repayment to HMSA of an amount that is no more than the lesser of the total Restorative Payments actually made by HMSA or the amount of litigation proceeds the Plan receives from the Claims, plus reasonable Attorney Fees paid to unrelated third parties by HMSA in connection with the Claims.

(d) The term "HMSA" means Hawaii Medical Service Association.

(e) The term "Independent Fiduciary" means Gallagher Fiduciary Advisors, LLC (Gallagher) or a successor Independent Fiduciary to the extent Gallagher or the successor Independent Fiduciary continues to serve in such capacity who:

(1) Is not an affiliate of HMSA and does not hold an ownership interest in HMSA or affiliates of HMSA;

(2) Was not a fiduciary with respect to the Plan before its appointment to serve as the Independent Fiduciary;

(3) Has acknowledged in writing that it:

(i) is a fiduciary with respect to the Plan and has agreed not to participate in any decision regarding any transaction in which it has an interest that might affect its best judgment as a fiduciary; and

(ii) Has appropriate technical training or experience to perform the services contemplated by the exemption;

(4) Has not entered into any agreement or instrument that violates the prohibitions on exculpatory provisions in ERISA Section 410 or the Department's regulation relating to indemnification of fiduciaries;<sup>50</sup>

(5) Has not received gross income from HMSA or its affiliates during any fiscal year in an amount that exceeds two percent (2%) of the Independent Fiduciary's gross income from all sources for the prior fiscal year. This provision also applies to a partnership or corporation of which the Independent Fiduciary is an officer, director, or 10 percent (10%) or more partner or shareholder, and includes as gross income amounts received as compensation for services provided as an independent fiduciary under any prohibited transaction exemption granted by the Department; and

(6) No organization or individual that is an Independent Fiduciary, and no partnership or corporation of which such organization or individual is an officer, director, or ten percent (10%) or more partner or

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<sup>50</sup> 29 CFR 2509.75-4.

shareholder, may acquire any property from, sell any property to, or borrow any funds from HMSA or from affiliates of HMSA while serving as an Independent Fiduciary. This prohibition will continue for six months after the party ceases to be an Independent Fiduciary and/or the Independent Fiduciary negotiates any transaction on behalf of the Plan during the period that the organization or individual serves as an Independent Fiduciary.

(f) The "Plan" means the Non-Contributory Retirement Program for Certain Employees of Hawaii Medical Service Association.

(g) The term "Plan Losses" means the \$187,271,581 in Plan losses the BCBSA's National Employee Benefits Committee alleges were the result of breaches of fiduciary responsibilities and breaches of contract by Allianz Global Investors U.S. LLC and/or Aon Investments USA Inc.

(h) The term "Restorative Payment" means the payment made by HMSA to the Plan in connection with the Plan Losses, defined above, consisting of a \$50,000,000 payment that HMSA contributed to the Plan on December 18, 2020. This \$50,000,000 payment is the Required Restorative Payment Amount.

(i) The "Repayment" means the payment, if any, that the Plan will transfer to HMSA following the Plan's receipt of proceeds from the Claims, where the Repayment is made

following the full and complete resolution of the Claims;  
and in a manner that is consistent with the terms of the  
exemption.

## **Section II. Proposed Transactions**

If the proposed exemption is granted, the restrictions of ERISA Sections 406(a)(1)(A) and (D) and the sanctions resulting from the application of Code Section 4975, by reason of Code Sections 4975(c)(1)(A) and (D), does not apply, effective November 3, 2020, to the following transactions: HMSA's transfer of Restorative Payment to the Plan; and, in return, the Plan's Repayment of an amount to HMSA, which must be no more than the lesser of the Restorative Payment Amount or the amount of litigation proceeds the Plan received from the Claims, plus reasonable Attorney Fees, provided that the Definitions set forth in Section I and the Conditions set forth in Section III are met.

## **Section III. Conditions**

(a) The Plan received the entire Restorative Payment on December 18, 2020;

(b) In connection with its receipt of the Restorative Payment, the Plan does not release any claims, demands and/or causes of action the Plan may have against the following: (1) any fiduciary of the Plan; (2) any

fiduciary of the Trust; (3) HMSA; and/or (4) any person or entity related to a person or entity identified in (1)-(3) of this paragraph;

(c) The Plan's Repayment to HMSA is for no more than the lesser of the total Restorative Payment received by the Plan or the amount of litigation proceeds the Plan receives from the Claims. The Plan's Repayment to HMSA may only occur after the Independent Fiduciary has determined that: all the conditions of the exemption are met; the Plan has received the Restorative Payment it is due; and the Plan has received all the litigation proceeds it is due. The Plan's Repayment to HMSA must be carried out in a manner designed to minimize unnecessary costs and disruption to the Plan and its investments;

(d) A qualified independent fiduciary (the Independent Fiduciary, as further defined in Section II(e)), acting solely on behalf of the Plan in full accordance with its obligations of prudence and loyalty under ERISA Sections 404(a)(1)(A) and (B) must:

(1) Review, negotiate and approve the terms and conditions of the Restorative Payment and the Repayment and the Contribution and Assignment Agreement, all of which must be in writing, before the Plan enters into those transactions/agreement;

(2) Determine that the Restorative Payment, the Repayment, and the terms of the Contribution and Assignment



Agreement, are prudent and in the interest of the Plan and its participants and beneficiaries;

(3) Confirm that the Required Restorative Payment Amount was fully and timely made;

(4) Monitor the litigation related to the Claims and confirm that the Plan receives, in a timely manner, its proper share of any litigation or settlement proceeds received by the Trust;

(5) Ensure that any Repayment by the Plan to HMSA for legal expenses in connection with the Claims is limited to only reasonable legal expenses that were paid by HMSA to unrelated third parties;

(6) Ensure that all of the conditions and definitions of this proposed exemption are met;

(7) Submit a written report to the Department's Office of Exemption Determinations demonstrating and confirming that the terms and conditions of the exemption were met, within 90 days after the Repayment; and

(8) Not enter into any agreement or instrument that violates ERISA Section 410 or the Department's Regulations codified at 29 CFR Section 2509.75-4.

(f) The Plan pays no interest in connection with the Restorative Payment;

(g) The Plan does not pledge any Plan assets to secure any portion of the Restorative Payment;

(h) The Plan does not incur any expenses, commissions, or transaction costs in connection with the Proposed Transactions. However, if first approved by the Independent Fiduciary, the Plan may reimburse HMSA for reasonable legal expenses paid in connection with the Claims by HAS to non-HMSA-related parties. For purposes of determining the amount of Attorney Fees the Plan may reimburse to HMSA under this proposal, the amount of reasonable attorney fees paid by HMSA on behalf of the Plan in connection with the Claims must be reduced by the amount of legal fees received by HMSA in connection with the Claims from any non-Plan party (i.e., pursuant to a court award);

(i) The proposed transactions do not involve any risk of loss to either the Plan or the Plan's participants and beneficiaries;

(j) No party associated with this exemption has or will indemnify the Independent Fiduciary and the Independent Fiduciary will not request indemnification from any party, in whole or in part, for negligence and/or any violation of state or federal law that may be attributable to the Independent Fiduciary in performing its duties to the Plan with respect to the Proposed Transactions. In addition, no contract or instrument may purport to waive any liability under state or federal law for any such violation.

(k) If an Independent Fiduciary resigns, is removed, or for any reason is unable to serve as an Independent Fiduciary, the Independent Fiduciary must be replaced by a successor entity that: (1) meets the definition of Independent Fiduciary detailed above in Section II(e); and (2) otherwise meets all of the qualification, independence, prudence and diligence requirements set forth in this exemption. Further, any such successor Independent Fiduciary must assume all of the duties of the outgoing Independent Fiduciary. As soon as possible, including before the appointment of a successor Independent Fiduciary, HMSA must notify the Department's Office of Exemption Determinations of the change in Independent Fiduciary and such notification must contain all material information regarding the successor Independent Fiduciary, including the successor Independent Fiduciary's qualifications; and

(1) All of the material facts and representations set forth in the Summary of Facts and Representation are true and accurate at all times.

#### NOTICE TO INTERESTED PERSONS

The Applicant will give notice of the proposed exemption to all interested persons and all of the parties to the litigation described above, within fifteen calendar days after the publication of the notice of proposed

exemption in the *Federal Register*. The notice will contain a copy of the notice of proposed exemption, as published in the *Federal Register*, and a supplemental statement, as required pursuant to the Department's regulations codified at 29 CFR 2570.43(a)(2). The supplemental statement will inform interested persons of their right to comment on the pending exemption. Written comments are due by [INSERT DATE THAT IS 45 DAYS FROM THE PUBLICATION OF THE NOTICE IN THE *FEDERAL REGISTER*].

All comments will be made available to the public.

**Warning:** If you submit a comment, EBSA recommends that you include your name and other contact information in the body of your comment, but DO NOT submit information that you consider to be confidential, or otherwise protected (such as a Social Security number or an unlisted phone number) or confidential business information that you do not want publicly disclosed. All comments may be posted on the Internet and can be retrieved by most Internet search engines.

*For Further Information Contact:* Mrs. Blessed Chuksorji-Keefe of the Department, telephone (202) 693-8567. (This is not a toll-free number.)

**BCS Financial Corporation**

**Located in Oakbrook Terrace, Illinois**

**[Application No. D-12036]**

## **Proposed Exemption**

The Department is considering granting an exemption under the authority of Section 408(a) of the Employee Retirement Income Security Act of 1974, as amended (ERISA), and Section 4975(c)(2) of the Internal Revenue Code of 1986, as amended (the Code). The proposed exemption relates to legal actions and claims (the Claims) against Allianz Global Investors U.S. LLC (Allianz) and Aon Investments USA Inc. (Aon), that arose from certain losses incurred by the Non-Contributory Retirement Program for Certain Employees of BCS Financial Corporation (the Plan) in the first quarter of 2020.<sup>51</sup>

This proposed exemption would permit the Plan sponsor, BCS Financial Corporation (BCS), to make a series of payments to the Plan, including: (a) past payments totaling \$19,600,000; and (b) a payment of \$1,800,000 on or before September 13, 2023 (the Restorative Payments). If the Plan receives litigation proceeds from the Claims, the Plan will transfer the lesser of the litigation proceeds amount or the Restorative Payments, plus reasonable attorney fees to BCS.

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<sup>51</sup> In proposing this exemption, the Department is not expressing an opinion regarding the merits of any Claim against Allianz and Aon, or whether the Plan's fiduciaries met their fiduciary duties with respect to Plan assets that are the subject of the Claims. Further, in proposing this exemption, the Department is not limiting any party's claim, demand and/or cause of action arising from the Plan's 2020 first quarter losses in any way. Among other things, this exemption preserves any right, claim, demand and/or cause of action the Plan may have against the following: (1) any fiduciary of the Plan; (2) any fiduciary of the Trust; (3) BCS Financial Corporation; and/or (4) any person or entity related to a person or entity described in (1)-(3).

## **SUMMARY OF FACTS AND REPRESENTATIONS<sup>52</sup>**

1. BCS is a not-for-profit company that provides health insurance products and services. BCS is wholly-owned by all of the primary licensees of Blue Cross Blue Shield Association (BCBSA) that are headquartered in Illinois.

2. The Plan is an ERISA-covered qualified defined benefit pension plan that covers eligible employees of BCS. On December 31, 2019, the Plan was closed to new entrants. As of December 31, 2020, the Plan covered 242 participants and held \$35,258,813 in total assets.

3. The Plan holds a beneficial interest in the Blue Cross and Blue Shield National Retirement Trust (the Trust). The Trust is a master trust that holds the assets of 16 defined benefit pension plans that participate in the BCBSA's National Retirement Program (the Participating Plans). Northern Trust serves as Trustee and asset custodian to the Trust and maintains separate records that reflect the net asset value of each Participating Plan.

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<sup>52</sup> The Department notes that availability of this exemption is subject to the express condition that the material facts and representations contained in application D-12036 are true and complete at all times and accurately describe all material terms of the transactions covered by the exemption. If there is any material change in a transaction covered by the exemption or in a material fact or representation described in the application, the exemption will cease to apply as of the date of such change. The Summary of Facts and Representations is based on the Applicant's representations, as well as factual representations contained in the Claims' cause of action (as described below) and does not reflect factual findings or opinions of the Department, unless indicated otherwise.

The Trust's earnings, market adjustments, and administrative expenses are allocated among the Participating Plans based on the respective Participating Plan's share of the Trust's assets. A Participating Plan's interest in the Trust's net assets is based on its share of the Trust.

4. The Committee serves as named fiduciary and administrator for each Participating Plan. The Committee is a standing committee of the BCBSA's board of directors. In 2011, the Committee invested a portion of the Trust's assets in funds managed by Allianz Global Investors U.S. LLC (Allianz), as part of a Structured Alpha Investment Strategy. These funds included: (a) AllianzGI Structured Alpha Multi-Beta Series LLC I; (b) AllianzGI Structured Alpha Emerging Markets Equity 350 LLC; and (c) AllianzGI Structured Alpha 1000 LLC (collectively, the Structured Alpha Funds).

5. The Applicant represents that the Allianz Structured Alpha strategy consisted of alpha and beta components. According to the applicant, the alpha component was an options trading strategy that Allianz claimed would seek targeted positive return potential while maintaining structural risk protections. The beta component was intended to provide broad market exposure to a particular asset class through investments in financial products similar to an exchange-traded fund that replicates

the performance of a market index, such as the S&P 500. According to the Applicant, Allianz represented that the Structured Alpha Strategy would capitalize on the return-generating features of option selling (short volatility) while simultaneously benefitting from the risk-control attributes associated with option buying (long volatility). According to the Applicant, Allianz represented further that the alpha component would include position hedging consisting of long-volatility positions designed to protect the portfolio in the event of a market crash.

6. As of December 31, 2019, the total market value of the Plan's portion of the Trust's investment in the Allianz Structured Alpha Funds was \$36,190,972, which represented 77.66% of total Plan assets.<sup>53</sup>

7. In 2009, the Committee retained Aon (then called Ennis Knupp) to provide investment advice regarding the investment of Plan assets held in the Trust. The Applicant represents that Aon provided regular investment advice pursuant to a written contract between it and the Committee. Pursuant to its engagement, Aon agreed to provide the following: "recommendations to [the Committee] regarding asset allocation" within the Trust; "recommendations to [the Committee] regarding the specific asset allocation and other investment guidelines" for the

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<sup>53</sup> By proposing this exemption, the Department does not, in any way, suggest a conclusion that the Plan's fiduciaries met their ERISA Section 404 duties when they caused the Trust to invest 77.66% of the Plan's total assets in the Allianz Structured Alpha Funds.



Trust's investment managers such as Allianz; and advice "regarding the diversification of assets" held in the Trust." The Applicant represents that Aon agreed to: conduct "active, ongoing monitoring" of Allianz to "identify any forward-looking" risks "that could impact performance;" and "inform itself" of any information necessary to discharge its duty to monitor, including information about the actual options positions Allianz had constructed.

8. The Applicant represents that when equity markets sharply declined in February and March of 2020, volatility spiked and the options positions held within the Structured Alpha Strategy were exposed to a heightened risk of loss. The Applicant represents that, unbeknownst to the Committee, and in violation of Allianz's stated investment strategy, Allianz abandoned the hedging strategy that was the supposed cornerstone of the Structured Alpha Strategy, leaving the portfolio almost entirely unhedged against a spike in market volatility. As described in the Claims, although Allianz had represented that it would buy hedges at strike prices ranging from 10% to 25% below the market, the hedges it actually held at the end of February 2020 were as much as 60% below the market.

The Applicant represents that, as of January 31, 2020, the Trust had invested approximately \$2,916,049,486 in the Structured Alpha Strategy. Six weeks later, the Trust

faced a margin call, which the Applicant states left it no choice but to liquidate the investment. The Trust was ultimately able to redeem only \$646,762,678 of its \$2,916,049,486 investment, resulting in a total loss of \$2,269,286,808.

Specifically, regarding the Plan's portion of the loss, as of December 31, 2019, the market value of the Plan was \$46,599,770. As of March 31, 2020, the market value of the Plan's total assets decreased to \$15,806,147. The Applicant represents that the Plan's total losses from the Allianz Structured Alpha Strategy were \$29,496,983, which caused the Plan to be underfunded.

9. On September 16, 2020, the Committee filed a cause of action in the United States District Court for the Southern District of New York (Case number 20-CIV-07606) against Allianz and Aon for Breach of Fiduciary Duty under ERISA Section 404, Breach of Co-Fiduciary Duty under ERISA Section 405, and violation of ERISA Section 406(b) for managing the Plan assets in its self-interest and breach of contract. It is possible that resolution of this claim and other legal actions against Allianz and Aon in connection with the Plan's losses (the Claims) could take an extended period of time.

10. The Applicant states that rather than wait for the Claims to be resolved, BCS took steps to protect Plan benefits and avoid onerous benefit restrictions under Code

section 436 that could apply to the Plan as a result of a funding shortfall. Therefore, on October 9, 2020, BCS and the Plan entered into a Contribution and Assignment Agreement (the Contribution and Assignment Agreement).

11. Pursuant to the Contribution and Assignment Agreement, BCS agreed to make a \$16,000,000 Restorative Payment to the Plan within seven business days after the Agreement's effective date. Subsequently, on October 13, 2020, BCS made a \$16,000,000 Restorative Payment to the Plan.

12. On September 27, 2021, BCS and the Plan amended the Restorative Payments provision of the Contribution and Assignment Agreement (the Restorative Payment Amendment). Pursuant to the amendment, BCS agreed to make the following three additional Restorative Payments to the Plan: (a) a payment of \$1,800,000 on or before September 13, 2021; (b) a payment of \$1,800,000 on or before September 13, 2022; and (c) a payment of \$1,800,000 on or before September 13, 2023. Since the effective date of the Restorative Payment Amendment, BCS Financial has made two additional Restorative Payments to the Plan: a \$1,800,000 payment on September 14, 2021, and a \$1,800,000 payment on January 14, 2022.

13. In exchange for the Restorative Payments, the Plan assigned to BCS its right to retain certain litigation and/or settlement proceeds recovered from the Claims (the

Assigned Interests).<sup>54</sup> Per the assignment, once the Allianz/Aon litigation is resolved and if the Plan receives litigation proceeds from the Claims, the Plan will transfer to BCS a repayment (the Repayment) that does not exceed the total Restorative Payments made by BCS, plus reasonable attorney fees paid by BCS on behalf of the Plan in connection with the Claims, if such fees are reviewed and approved by a qualified independent fiduciary who confirms that the fees were reasonably incurred and paid by BCS to unrelated third parties (the Attorney Fees). For the purposes of this exemption, Attorney Fees reimbursable to BCS do not include: (a) legal expenses paid by the Plan; and (b) legal expenses paid by BCS for representation of its own interests or the interests of any party other than the Plan. For purposes of determining the amount of Attorney Fees the Plan may reimburse to BCS under this exemption, the amount of reasonable attorney fees paid by BCS on behalf of the Plan in connection with the Claims must be reduced by the amount of legal fees received by BCS in connection with the Claims from any non-Plan party (for example, from a third party pursuant to a court award).

14. The Plan must ultimately receive at least the full value of the promised Restorative Payments, minus the

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<sup>54</sup> Under the Contribution and Assignment Agreement, if the Plan receives litigation or settlement proceeds from the Claims, the proceeds would first flow to the Trust, and then each Plan's pro rata portion of the proceeds would be deposited into the individual trust funding that Plan.

Attorney Fees. The Plan may ultimately receive more than the Restorative Payment amount required under the Contribution and Assignment Agreement. If the Plan receives litigation or settlement proceeds that exceed the amount of Restorative Payments that BCS has made to the Plan, the Plan's Repayment to BCS will be limited to the amount of Restorative Payments actually made by BCS, plus Attorney Fees. For example, if BCS has made \$19,600,000 in Restorative Payments to the Plan and reasonably incurred \$100,000 in Attorney Fees, and if the Plan receives \$30,000,000 in litigation proceeds, the Plan will make a Repayment to BCS totaling \$19,700,000.

15. Alternatively, if the Plan receives less litigation or settlement proceeds than the amount of Restorative Payments that BCS has made to the Plan, the Plan will transfer to BCS the lesser amount of litigation or settlement proceeds, plus Attorney Fees. For example, if BCS has made \$19,600,000 in Restorative Payments to the Plan and has reasonably incurred \$100,000 in Attorney Fees, and if the Plan receives \$10,000,000 in litigation proceeds, the Plan will make a Repayment to BCS totaling \$10,100,000.

16. The Department notes that if the Plan receives any restitution that is tied to the conduct underlying the Claims but was ordered pursuant to a proceeding or directive that is external to Case number 20-CIV-07606, the

disposition of such proceeds must conform to the requirements of this exemption.

17. BCS retained Gallagher Fiduciary Advisors, LLC (Gallagher or the Independent Fiduciary) of New York, New York, to serve as the Plan's independent fiduciary with respect to the Required Restorative Payments and the potential repayment by the Plan of those Payments (collectively, the Proposed Transactions). Gallagher represents that it has extensive experience in institutional investment consulting and fiduciary decision-making regarding traditional and alternative investments. Gallagher further represents that its independent fiduciary decision-making work involves acting as a fiduciary advisor or decision-maker for plans and other ERISA-regulated asset pools and that it has experience with a wide range of asset classes and litigation claims.

18. Gallagher represents that it understands its duties and responsibilities under ERISA in acting as a fiduciary on behalf of the Plan. Gallagher also acknowledges that it is authorized to take all appropriate actions to safeguard the Plan's interests, and that it will monitor the Proposed Transactions on the Plan's behalf on a continuous basis and throughout the term required by this exemption.

19. Gallagher represents that it does not have any prior relationship with any parties in interest to the

Plan, including BCS and any BCS affiliates. Gallagher further represents the total revenues it has received from the Plan and from parties in interest to the Plan in connection with its engagement as Independent Fiduciary represents approximately 0.78% of Gallagher's total revenue.

20. Gallagher represents that no party associated with this exemption application has or will indemnify it, in whole or in part, for negligence of any kind and/or any violation of state or federal law that may be attributable to Gallagher's performance of its duties as Independent Fiduciary to the Plan with respect to the Proposed Transactions. In addition, no contract or instrument entered into by Gallagher as Independent Fiduciary may purport to waive any liability under state or federal law for any such violation.

21. On October 9, 2020, Gallagher completed an Independent Fiduciary Report (the Independent Fiduciary Report) finding that the massive losses caused by the Trust's investment in the Allianz Structured Alpha Strategy resulted in a significant reduction to the Plan's total assets and funding level. Gallagher represents that the Required Restorative Payments, which will be received by the Plan substantially in advance of a final resolution of the Claims against Allianz and Aon, should restore the Plan's funded percentage to its pre-loss funded percentage

as of January 1, 2019. The restoration of the Plan's funding status will secure ongoing benefit payments to participants and beneficiaries.

Gallagher notes that the Contribution and Assignment Agreement provides that the Trust must reimburse BCS only up to the Required Restorative Payment Amount, plus any reasonable legal expense paid to non-BCS-related parties that were incurred by, or allocated to, BCS as a result of the Claims.<sup>55</sup> Thus, if the Plan's ultimate recovery amount from the Claims is less than the Required Restorative Payment Amount, plus related litigation expenses that were allocated to the Plan, BCS, not the Plan, will suffer the loss.

Gallagher states that the Proposed Transactions and the terms of the Contribution and Assignment Agreement were negotiated and approved by Gallagher in its role as the Plan's Independent Fiduciary. Gallagher states that it approved the Proposed Transactions only after conducting an extensive analysis of the damages suffered by the Plan as a result of the failed Allianz Structured Alpha Strategy. Gallagher represents that it conducted numerous discussions with Trust representatives and counsel, along with the

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<sup>55</sup> Currently, legal fees and expenses associated with the Claims are being paid by most of the Participating Plan's trusts on a pro rata basis according to each Participating Plan's total invested assets held in the Master Trust's Allianz Structured Alpha Strategy before the losses were incurred in the first quarter 2020. The Applicant represents that the Committee reviews and approves these legal fees before passing them through to each Participating Plan.



Plan's representatives and counsel to ensure that the interests of the Plan's participants and beneficiaries were protected with respect to all aspects of the Proposed Transactions. Based upon its assessment, Gallagher approved the Plan's receipt of the Required Restorative Payments from BCS in exchange for the Assignment.

#### ERISA Analysis

22. Absent an exemption, the Plan's receipt of the Restorative Payments from BCS in exchange for the Plan's transfer of litigation or settlement proceeds to BCS would violate ERISA. In this regard, ERISA Section 406(a)(1)(A) prohibits a plan fiduciary from causing the plan to engage in a transaction if the fiduciary knows or should know that such transaction constitutes a direct or indirect sale or exchange of any property between a plan and a party in interest. BCS, as an employer whose employees are covered by the Plan, is a party in interest with respect to the Plan under ERISA Section 3(14)(C). The Required Restorative Payments to the Plan and the Plan's potential repayment to BCS with litigation or settlement proceeds would constitute impermissible exchanges between the Plan and a party-in-interest (BCS) in violation of ERISA Section 406(a)(1)(A).

ERISA Section 406(a)(1)(B) prohibits the lending of money or other extension of credit between a plan and a

party-in-interest. BCS's promise to make Required Restorative Payments to the Plan, over time, constitutes an impermissible extension of credit between the Plan and a party-in-interest in violation of ERISA Section 406(a) (1) (B) .

ERISA Section 406(a) (1) (D) prohibits a plan fiduciary from causing a plan to engage in a transaction if the fiduciary knows or should know that the transaction constitutes a direct or indirect transfer to, or use by or for the benefit of, a party-in-interest, of the income or assets of the plan. The transfer of Plan assets to BCS in connection with the Repayment would constitute an impermissible transfer of Plan assets to a party-in-interest in violation of ERISA Section 406(a) (1) (D) .

#### Conditions

23. This proposed exemption contains a number of conditions that must be met. For example, the proposed exemption mandates that the Independent Fiduciary, in full accordance with its obligations of prudence and loyalty under ERISA Section 404(a) (1) (A) and (B) must:

(a) review, negotiate, and approve the terms and conditions of the Required Restorative Payments, the Repayment, and the Contribution and Assignment Agreement, before the Plan enters into such payments and the agreement;

(b) determine that the terms and conditions of the Required Restorative Payments, the Repayment, and the Contribution and Assignment Agreement are prudent, in the interest of the Plan and its participants and beneficiaries, and protective of the rights of the Plan's participants and beneficiaries;

(c) confirm that the Required Restorative Payments are fully and timely made;

(d) monitor the Claims and confirm that the Plan receives its proper share of any litigation or settlement proceeds received by the Trust in connection with the Claims;

(e) ensure that any Repayment by the Plan to BCS fully complies with the terms of this exemption and is for no more than the lesser of the total Restorative Payments actually made to the Plan by BCS or the amount the Plan received from the Claims, plus Attorney Fees;

(f) ensure that any Repayment by the Plan to BCS for legal expenses in connection with the Claims is limited to only reasonable legal expenses that were paid by BCS to unrelated third parties for representation of the Plan and its interests (as opposed to representation of BCS or the interests of any party other than the Plan) where BCS was not otherwise reimbursed from a non-Plan party;

(g) monitor the Plan's Assigned Interests on an ongoing basis to determine and confirm that any excess

recovery amount from the Claims (i.e., any amount that exceeds the Required Restorative Payment Amount) is retained by the Plan;

(h) ensure that all of the conditions and definitions of this proposed exemption are met; and

(i) represent that it has not and will not enter into any agreement or instrument that violates ERISA Section 410 or Department Regulations codified at 29 CFR section 2509.75-4.<sup>56</sup>

24. This proposed exemption also requires Gallagher to respond in writing to any information requests from the Department regarding Gallagher's activities as the Plan's Independent Fiduciary. Additionally, no later than 90 days after the resolution of the litigation, Gallagher must submit a written report to the Department demonstrating that all terms and conditions of the exemption have been met.

25. This proposed exemption requires that the Plan has not and will not release any claims, demands and/or causes of action it may have against: (a) any fiduciary of the Plan; (b) any fiduciary of the Trust; (c) BCS; and/or (d) any person or entity related to a person or entity described in (a)-(c) of this paragraph. Additionally, any

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<sup>56</sup> ERISA Section 410 provides, in part, that "except as provided in ERISA Sections 405(b)(1) and 405(d), any provision in an agreement or instrument which purports to relieve a fiduciary from responsibility or liability for any responsibility, obligation, or duty under this part [meaning Part 4 of Title I of ERISA] shall be void as against public policy."

Repayment by the Plan to BCS must be made in a manner designed to minimize unnecessary costs and disruption to the Plan and its investments.

26. The Plan may not make any Repayment to BCS before the date: the Plan has received from BCS the entire amount of the Restorative Payments agreed to in the Amended Contribution and Assignment Agreement; and all the Claims are settled. Furthermore, the Plan may not pay any interest to BCS in connection with its receipt of the Required Restorative Payments, nor pledge Plan assets to secure any portion of the Required Restorative Payments.

27. Pursuant to this proposed exemption, the Plan may not incur any expenses, commissions or transaction costs in connection with the Proposed Transactions. However, as noted above, under certain circumstances the Plan may reimburse BCS for reasonable legal expenses arising from the Claims that BCS paid to non-BCS-related parties for representation of the Plan and its interests (as opposed to representation of BCS or the interests of any party other than the Plan) where BCS was not otherwise reimbursed by a non-Plan party.

28. Finally, the exemptive relief provided under this proposed exemption is conditioned upon the Department's assumption that the material facts and representations set forth above in the Summary of Facts and Representation section are true and accurate at all times. In the event

that a material fact or representation detailed above is untrue or inaccurate, the exemptive relief provided under this exemption will cease immediately.

### Statutory Findings

29. ERISA Section 408(a) provides, in part, that the Department may not grant an exemption unless the Department finds that the exemption is administratively feasible, in the interest of affected plans and of their participants and beneficiaries, and protective of the rights of such participants and beneficiaries. Each of these criteria is discussed below.

a. The Proposed Exemption Is "Administratively Feasible." The Department has tentatively determined that the proposed exemption is administratively feasible because, among other things, the Independent Fiduciary will represent the interests of the Plan for all purposes with respect to the Proposed Transactions.<sup>57</sup> In this regard, not later than 90 days after the resolution of the litigation, the Independent Fiduciary must submit a written report to the Department demonstrating that all of the requirements of this exemption have been met.

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<sup>57</sup> This proposed exemption would require that if the Independent Fiduciary resigns, is removed, or for any reason is unable to serve as an Independent Fiduciary, the successor Independent Fiduciary must, among other things, assume all of the duties of the outgoing Independent Fiduciary. As soon as possible, including before the appointment of a successor Independent Fiduciary, the Plan Sponsor and the Plan must notify the Department's Office of Exemption Determinations of the change in Independent Fiduciaries. The notification must contain all material information including the qualifications of the successor Independent Fiduciary.

b. The Proposed Exemption Is "In the Interests of the Plan." The Department has tentatively determined that the proposed exemption is in the interest of the Plan because, among other things, the Plan's receipt of the Required Restorative Payments will substantially improve the Plan's funding status, which will enhance the Plan's ability to meet its obligations to fund benefit obligations to participants and beneficiaries and help the Plan avoid the imposition of benefit limitations imposed under Code section 436.

c. The Proposed Exemption Is "Protective of the Plan." The Department has tentatively determined that the proposed exemption is protective of the rights of the Plan's participants and beneficiaries because, among other things, the Plan will repay BCS the lesser of the Required Restorative Payment Amount, or the amount the Plan receives in proceeds from the Claims, ensuring that the Proposed Transactions will result in an increase in Plan assets of at least the total amount of Restorative Payments (less reasonable legal expenses related to the Claims paid by BCS to unrelated third parties, as confirmed and approved by the Independent Fiduciary). Further, this exemption preserves any right, claim, demand and/or cause of action the Plan may have against: (a) any fiduciary of the Plan; (b) any fiduciary of the Trust; (c) BCS; and/or (d) any person or entity related to a person or entity described in (a)-(c).

### Summary

30. Based on the conditions described above, the Department has tentatively determined that the relief sought by the Applicant satisfies the statutory requirements under ERISA Section 408(a) for the Department to make findings that support its issuance of a proposed exemption.

### **PROPOSED EXEMPTION**

The Department is considering granting an exemption under the authority of ERISA Section 408(a) and Code Section 4975(c)(2) and in accordance with the procedures set forth in the Department's exemption procedure regulation.<sup>58</sup>

### **Section I. Definitions**

(a) The term "Attorney Fees" means reasonable legal expenses paid by BCS on behalf of the Plan in connection with the Claims, if such fees are reviewed and approved by a qualified independent fiduciary who confirms that the fees were reasonably incurred and paid by BCS to unrelated third parties. For the purposes of this exemption, the Attorney Fees reimbursable to BCS do not include: (1) legal expenses paid by the Plan; and (2) legal expenses paid by BCS for representation of BCS or the interests of any party other than the Plan.

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<sup>58</sup> 29 CFR part 2570, subpart B (55 FR 32836, 32847, August 10, 1990).



(b) The term "BCS" means BCS Financial Corporation.

(c) The term "Claims" means the legal claims against Allianz Global Investors U.S. LLC (Allianz) and Aon Investments USA Inc. (Aon), to recover certain losses incurred by the Plan in the first quarter of 2020.

(d) The term "Contribution and Assignment Agreement" means the written agreement between BCS and the Plan, dated October 9, 2020, and its amendment that became effective on September 27, 2021, containing all material terms regarding BCS's agreement to make Required Restorative Payments (as described in Section I(h)) to the Plan in return for the Plan's potential Repayment to BCS of an amount that is no more than the lesser of the total Restorative Payments or the amount of litigation proceeds the Plan receives from the Claims, plus reasonable Attorney Fees paid to unrelated third parties by BCS in connection with the Claims.

(e) The term "Independent Fiduciary" means Gallagher Fiduciary Advisors, LLC (Gallagher) or a successor Independent Fiduciary to the extent Gallagher or the successor Independent Fiduciary continues to serve in such capacity who:

(1) Is not an affiliate of BCS and does not hold an ownership interest in BCS or affiliates of BCS;

(2) Was not a fiduciary with respect to the Plan before its appointment to serve as the Independent Fiduciary;

(3) Has acknowledged in writing that it:

(i) is a fiduciary with respect to the Plan and has agreed not to participate in any decision regarding any transaction in which it has an interest that might affect its best judgment as a fiduciary; and

(ii) Has appropriate technical training or experience to perform the services contemplated by the exemption;

(4) Has not entered into any agreement or instrument that violates the prohibitions on exculpatory provisions in ERISA Section 410 or the Department's regulation relating to indemnification of fiduciaries;<sup>59</sup>

(5) Has not received gross income from BCS or its affiliates during any fiscal year in an amount that exceeds two percent (2%) of the Independent Fiduciary's gross income from all sources for the prior fiscal year. This provision also applies to a partnership or corporation of which the Independent Fiduciary is an officer, director, or 10 percent (10%) or more partner or shareholder, and includes as gross income amounts received as compensation for services provided as an independent fiduciary under any prohibited transaction exemption granted by the Department; and

(6) No organization or individual that is an Independent Fiduciary, and no partnership or corporation of which such organization or individual is an officer,

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<sup>59</sup> 29 CFR 2509.75-4.

director, or ten percent (10%) or more partner or shareholder, may acquire any property from, sell any property to, or borrow any funds from BCS or from affiliates of BCS while serving as an Independent Fiduciary. This prohibition will continue for six months after the party ceases to be an Independent Fiduciary and/or the Independent Fiduciary negotiates any transaction on behalf of the Plan during the period that the organization or individual serves as an Independent Fiduciary.

(f) The "Plan" means the Non-Contributory Retirement Program for Certain Employees of BCS Financial Corporation.

(g) The term "Plan Losses" means the \$29,496,983 in Plan losses the BCBSA's National Employee Benefits Committee alleges were the result of breaches of fiduciary responsibilities and breaches of contract by Allianz Global Investors U.S. LLC and/or Aon Investments USA Inc.

(h) The term "Restorative Payments" means the payments made by BCS in connection with the Plan Losses, defined above, consisting of: (1) the past payment of \$16,000,000, made on October 13, 2020; (2) the past payment of \$1,800,000, made on September 14, 2021; (3) the past payment of \$1,800,000 made on January 14, 2022; and (4) a payment of \$1,800,000 to be made on or before September 13, 2023. The sum of (1)-(4) is the Required Restorative Payment Amount.

(i) The "Repayment" means the payment, if any, that the Plan will transfer to BCS following the Plan's receipt of proceeds from the Claims, where the Repayment is made following the full and complete resolution of the Claims; and in a manner that is consistent with the terms of the exemption.

## **Section II. Proposed Transactions**

If the proposed exemption is granted, the restrictions of ERISA Sections 406(a)(1)(A), (B) and (D) and the sanctions resulting from the application of Code Section 4975, by reason of Code Sections 4975(c)(1)(A), (B) and (D), shall not apply, effective October 9, 2020, to the following transactions: BCS's transfer of Restorative Payments to the Plan; and, in return, the Plan's Repayment of an amount to BCS, which must be no more than the lesser of the Restorative Payment Amount or the amount of litigation proceeds the Plan received from the Claims, plus reasonable Attorney Fees, provided that the Definitions set forth in Section I and the Conditions set forth in Section III are met.

## **Section III. Conditions**

(a) The Plan receives the entire Restorative Payment Amount no later than September 13, 2023;

(b) In connection with its receipt of the Required Restorative Payments, the Plan does not release any claims, demands and/or causes of action the Plan may have against the following: (1) any fiduciary of the Plan; (2) any fiduciary of the Trust; (3) BCS; and/or (4) any person or entity related to a person or entity identified in (1)-(3) of this paragraph;

(c) The Plan's Repayment to BCS is for no more than the lesser of the total Restorative Payments received by the Plan or the amount of litigation proceeds the Plan receives from the Claims. The Plan's Repayment to BCS may only occur after the Independent Fiduciary has determined that: all the conditions of the exemption are met; the Plan has received all the Restorative Payments it is due; and the Plan has received all the litigation proceeds it is due. The Plan's Repayment to BCS must be carried out in a manner designed to minimize unnecessary costs and disruption to the Plan and its investments;

(d) A qualified independent fiduciary (the Independent Fiduciary, as further defined in Section II(e)), acting solely on behalf of the Plan in full accordance with its obligations of prudence and loyalty under ERISA Sections 404(a)(1)(A) and (B) must:

(1) Review, negotiate and approve the terms and conditions of the Restorative Payments and the Repayment and the Contribution and Assignment Agreement, all of which

must be in writing, before the Plan enters into those transactions/agreement;

(2) Determine that the Restorative Payments, the Repayment, and the terms of the Contribution and Assignment Agreement, are prudent and in the interest of the Plan and its participants and beneficiaries;

(3) Confirm that the Required Restorative Payment Amount was fully and timely made;

(4) Monitor the litigation related to the Claims and confirm that the Plan receives, in a timely manner, its proper share of any litigation or settlement proceeds received by the Trust;

(5) Ensure that any Repayment by the Plan to BCS for legal expenses in connection with the Claims is limited to only reasonable legal expenses that were paid by BCS to unrelated third parties;

(6) Ensure that all of the conditions and definitions of this proposed exemption are met;

(7) Submit a written report to the Department's Office of Exemption Determinations demonstrating and confirming that the terms and conditions of the exemption were met, within 90 days after the Repayment; and

(8) Not enter into any agreement or instrument that violates ERISA Section 410 or the Department's Regulations codified at 29 CFR Section 2509.75-4.

(f) The Plan pays no interest in connection with the Restorative Payments;

(g) The Plan does not pledge any Plan assets to secure any portion of the Restorative Payments;

(h) The Plan does not incur any expenses, commissions, or transaction costs in connection with the Proposed Transactions. However, if first approved by the Independent Fiduciary, the Plan may reimburse BCS for reasonable legal expenses paid in connection with the Claims by BCS to non-BCS-related parties. For purposes of determining the amount of Attorney Fees the Plan may reimburse to BCS under this proposal, the amount of reasonable attorney fees paid by BCS on behalf of the Plan in connection with the Claims must be reduced by the amount of legal fees received by BCS in connection with the Claims from any non-Plan party (i.e., pursuant to a court award);

(i) The proposed transactions do not involve any risk of loss to either the Plan or the Plan's participants and beneficiaries;

(j) No party associated with this exemption has or will indemnify the Independent Fiduciary and the Independent Fiduciary will not request indemnification from any party, in whole or in part, for negligence and/or any violation of state or federal law that may be attributable to the Independent Fiduciary in performing its duties to the Plan with respect to the Proposed Transactions. In

addition, no contract or instrument may purport to waive any liability under state or federal law for any such violation.

(k) If an Independent Fiduciary resigns, is removed, or for any reason is unable to serve as an Independent Fiduciary, the Independent Fiduciary must be replaced by a successor entity that: (1) meets the definition of Independent Fiduciary detailed above in Section II(e); and (2) otherwise meets all of the qualification, independence, prudence and diligence requirements set forth in this exemption. Further, any such successor Independent Fiduciary must assume all of the duties of the outgoing Independent Fiduciary. As soon as possible, including before the appointment of a successor Independent Fiduciary, BCS must notify the Department's Office of Exemption Determinations of the change in Independent Fiduciary and such notification must contain all material information regarding the successor Independent Fiduciary, including the successor Independent Fiduciary's qualifications; and

(l) All of the material facts and representations set forth in the Summary of Facts and Representation are true and accurate at all times.

NOTICE TO INTERESTED PERSONS



The Applicant will give notice of the proposed exemption to all interested persons and all of the parties to the litigation described above, within fifteen calendar days after the publication of the notice of proposed exemption in the *Federal Register*. The notice will contain a copy of the notice of proposed exemption, as published in the *Federal Register*, and a supplemental statement, as required pursuant to the Department's regulations codified at 29 CFR 2570.43(a)(2). The supplemental statement will inform interested persons of their right to comment on the pending exemption. Written comments are due by [INSERT DATE THAT IS 45 DAYS FROM THE PUBLICATION OF THE NOTICE IN THE *FEDERAL REGISTER*].

All comments will be made available to the public.

**Warning:** If you submit a comment, EBSA recommends that you include your name and other contact information in the body of your comment, but DO NOT submit information that you consider to be confidential, or otherwise protected (such as a Social Security number or an unlisted phone number) or confidential business information that you do not want publicly disclosed. All comments may be posted on the Internet and can be retrieved by most Internet search engines.

*For Further Information Contact:* Mr. Frank Gonzalez of the Department, telephone (202) 693-8553. (This is not a toll-free number.)

**Blue Cross and Blue Shield of Mississippi, A Mutual  
Insurance Company  
Located in Flowood, Mississippi  
[Application No. D-12040]**

**Proposed Exemption**

The Department is considering granting an exemption under the authority of Section 408(a) of the Employee Retirement Income Security Act of 1974, as amended (ERISA), and Section 4975(c)(2) of the Internal Revenue Code of 1986, as amended (the Code). The proposed exemption relates to legal actions and claims (the Claims) against Allianz Global Investors U.S. LLC (Allianz) and Aon Investments USA Inc. (Aon), that arose from certain losses incurred by the Non-Contributory Retirement Program for Certain Employees of Blue Cross and Blue Shield of Mississippi (the Plan) in the first quarter of 2020.<sup>60</sup>

This proposed exemption would permit the past payments of \$70,000,000 and \$12,000,000 by the Plan sponsor, Blue

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<sup>60</sup> In proposing this exemption, the Department is not expressing an opinion regarding the merits of any Claim against Allianz and Aon, or whether the Plan's fiduciaries met their fiduciary duties with respect to Plan assets that are the subject of the Claims. Further, in proposing this exemption, the Department is not limiting any party's claim, demand and/or cause of action arising from the Plan's 2020 first quarter losses in any way. Among other things, this exemption preserves any right, claim, demand and/or cause of action the Plan may have against the following: (1) any fiduciary of the Plan; (2) any fiduciary of the Trust; (3) Blue Cross and Blue Shield of Mississippi, a Mutual Insurance Company; and/or (4) any person or entity related to a person or entity described in (1)-(3).

Cross and Blue Shield of Mississippi, A Mutual Insurance Company (BCBS MS), to the Plan (the Restorative Payments). If the Plan receives litigation proceeds from the Claims, the Plan will transfer the lesser of the litigation proceeds amount or the Restorative Payments, plus reasonable attorney fees to BCBS MS.

### **SUMMARY OF FACTS AND REPRESENTATIONS<sup>61</sup>**

1. BCBS MS is a not-for-profit company that provides health insurance products and services. BCBS MS is an independent licensee of the Blue Cross Blue Shield Association (BCBSA).

2. The Plan is an ERISA-covered qualified defined benefit pension plan that covers eligible employees of BCBS MS and employees of affiliated employers. As of December 31, 2006, the Plan was closed to new entrants. As of December 31, 2020, the Plan covered 976 participants and held \$153,536,775 in total assets.

3. The Plan holds a beneficial interest in the Blue Cross and Blue Shield National Retirement Trust (the

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<sup>61</sup> The Department notes that availability of this exemption is subject to the express condition that the material facts and representations contained in application D-12040 are true and complete at all times and accurately describe all material terms of the transactions covered by the exemption. If there is any material change in a transaction covered by the exemption or in a material fact or representation described in the application, the exemption will cease to apply as of the date of such change. The Summary of Facts and Representations is based on the Applicant's representations, as well as factual representations contained in the Claims' cause of action (as described below) and does not reflect factual findings or opinions of the Department, unless indicated otherwise.

Trust). The Trust is a master trust that holds the assets of 16 defined benefit pension plans that participate in the BCBSA's National Retirement Program (the Participating Plans). Northern Trust serves as Trustee and asset custodian to the Trust and maintains separate records that reflect the net asset value of each Participating Plan. The Trust's earnings, market adjustments, and administrative expenses are allocated among the Participating Plans based on the respective Participating Plan's share of the Trust's assets. A Participating Plan's interest in the Trust's net assets is based on its share of the Trust.

4. The Committee serves as named fiduciary and administrator for each Participating Plan. The Committee is a standing committee of the BCBSA's board of directors. In 2011, the Committee invested a portion of the Trust's assets in funds managed by Allianz Global Investors U.S. LLC (Allianz), as part of a Structured Alpha Investment Strategy. These funds included: (a) AllianzGI Structured Alpha Multi-Beta Series LLC I; (b) AllianzGI Structured Alpha Emerging Markets Equity 350 LLC; and (c) AllianzGI Structured Alpha 1000 LLC (collectively, the Structured Alpha Funds).

5. The Applicant represents that the Allianz Structured Alpha strategy consisted of alpha and beta components. According to the applicant, the alpha

component was an options trading strategy that Allianz claimed would seek targeted positive return potential while maintaining structural risk protections. The beta component was intended to provide broad market exposure to a particular asset class through investments in financial products similar to an exchange-traded fund that replicates the performance of a market index, such as the S&P 500. According to the Applicant, Allianz represented that the Structured Alpha Strategy would capitalize on the return-generating features of option selling (short volatility) while simultaneously benefitting from the risk-control attributes associated with option buying (long volatility). According to the Applicant, Allianz represented further that the alpha component would include position hedging consisting of long-volatility positions designed to protect the portfolio in the event of a market crash.

6. As of December 31, 2019, the total market value of the Plan's portion of the Trust's investment in the Allianz Structured Alpha Funds was \$122,962,882, which represented 71.18% of total Plan assets.<sup>62</sup>

7. In 2009, the Committee retained Aon (then called Ennis Knupp) to provide investment advice regarding the investment of Plan assets held in the Trust. The Applicant represents that Aon provided regular investment advice

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<sup>62</sup> By proposing this exemption, the Department does not, in any way, suggest a conclusion that the Plan's fiduciaries met their ERISA Section 404 duties when they caused the Trust to invest 71.18% of the Plan's total assets in the Allianz Structured Alpha Funds.

pursuant to a written contract between it and the Committee. Pursuant to its engagement, Aon agreed to provide the following: "recommendations to [the Committee] regarding asset allocation" within the Trust; "recommendations to [the Committee] regarding the specific asset allocation and other investment guidelines" for the Trust's investment managers such as Allianz; and advice "regarding the diversification of assets" held in the Trust." The Applicant represents that Aon agreed to: conduct "active, ongoing monitoring" of Allianz to "identify any forward-looking" risks "that could impact performance;" and "inform itself" of any information necessary to discharge its duty to monitor, including information about the actual options positions Allianz had constructed.

8. The Applicant represents that when equity markets sharply declined in February and March of 2020, volatility spiked and the options positions held within the Structured Alpha Strategy were exposed to a heightened risk of loss. The Applicant represents that, unbeknownst to the Committee, and in violation of Allianz's stated investment strategy, Allianz abandoned the hedging strategy that was the supposed cornerstone of the Structured Alpha Strategy, leaving the portfolio almost entirely unhedged against a spike in market volatility. As described in the Claims, although Allianz had represented that it would buy hedges

at strike prices ranging from 10% to 25% below the market, the hedges it actually held at the end of February 2020 were as much as 60% below the market.

The Applicant represents that, as of January 31, 2020, the Trust had invested approximately \$2,916,049,486 in the Structured Alpha Strategy. Six weeks later, the Trust faced a margin call, which the Applicant states left it no choice but to liquidate the investment. The Trust was ultimately able to redeem only \$646,762,678 of its \$2,916,049,486 investment, resulting in a total loss of \$2,269,286,808.

Specifically, regarding the Plan's portion of the loss, as of December 31, 2019 the market value of Plan assets was \$172,731,750. As of March 31, 2020, the market value of Plan assets decreased to \$67,238,446. The Applicant represents that the Plan's total losses from the Allianz Structured Alpha Strategy were \$102,446,155, which caused the Plan to be underfunded.

9. On September 16, 2020, the Committee filed a cause of action in the United States District Court for the Southern District of New York (Case number 20-CIV-07606) against Allianz and Aon for Breach of Fiduciary Duty under ERISA Section 404, Breach of Co-Fiduciary Duty under ERISA Section 405, and violation of ERISA Section 406(b) for managing the Plan assets in its self-interest and breach of contract. It is possible that resolution of this claim and

other legal actions against Allianz and Aon in connection with the Plan's losses (the Claims) could take an extended period of time.

10. The Applicant states that rather than wait for the Claims to be resolved, BCBS MS took steps to protect Plan benefits and avoid onerous benefit restrictions under Code section 436 that could apply to the Plan as a result of a funding shortfall. Therefore, on September 17, 2020, BCBS MS and the Plan entered into a Contribution and Assignment Agreement (the Contribution and Assignment Agreement).

11. Pursuant to the Contribution and Assignment Agreement, BCBS MS agreed to make the following Restorative Payments to the Plan: (a) a \$70,000,000 payment within seven business days of the effective date of the Contribution and Assignment Agreement; and (b) a \$12,000,000 payment on or about November 24, 2020. BCBS MS subsequently made the following Restorative Payments to the Plan: (a) a payment of \$70,000,000 on September 21, 2020; and (b) a payment of \$12,000,000 on November 25, 2020.

12. In exchange for the Restorative Payments, the Plan assigned to BCBS MS its right to retain certain litigation and/or settlement proceeds recovered from the Claims (the Assigned Interests).<sup>63</sup> Per the assignment, once

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<sup>63</sup> Under the Contribution and Assignment Agreement, if the Plan receives litigation or settlement proceeds from the Claims, the proceeds would first flow to the Trust, and then each Plan's pro rata portion of the



the Allianz/Aon litigation is resolved and if the Plan receives litigation proceeds from the Claims, the Plan will transfer to BCBS MS a repayment (the Repayment) that does not exceed the total Restorative Payments made by BCBS MS as of that date, plus reasonable attorney fees paid by BCBS MS on behalf of the Plan in connection with the Claims, if such fees are reviewed and approved by a qualified independent fiduciary who confirms that the fees were reasonably incurred and paid by BCBS MS to unrelated third parties (the Attorney Fees).

For the purposes of this exemption, Attorney Fees reimbursable to BCBS MS do not include: (a) legal expenses paid by the Plan; and (b) legal expenses paid by BCBS MS for representation of its own interests or the interests of any party other than the Plan. For purposes of determining the amount of Attorney Fees the Plan may reimburse to BCBS MS under this exemption, the amount of reasonable attorney fees paid by BCBS MS on behalf of the Plan in connection with the Claims must be reduced by the amount of legal fees received by BCBS MS in connection with the Claims from any non-Plan party (for example, from a third party pursuant to a court award).

13. The Plan must ultimately receive at least the full value of the promised Restorative Payments, minus the

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proceeds would be deposited into the individual trust funding that Plan.

Attorney Fees. The Plan, however, may ultimately receive more than the Restorative Payment amount required under the Contribution and Assignment Agreement. If the Plan receives litigation or settlement proceeds that exceed the amount of Restorative Payments that BCBS MS has made to the Plan, the Plan's Repayment to BCBS MS will be limited to the amount of Restorative Payments actually made by BCBS MS, plus Attorney Fees. For example, if BCBS MS reasonably incurred \$100,000 in Attorney Fees, and the Plan receives \$100,000,000 in litigation proceeds, the Plan will make a Repayment to BCBS MS totaling \$82,100,000.

14. Alternatively, if the Plan receives less litigation or settlement proceeds than the amount of Restorative Payments that BCBS MS has made to the Plan, the Plan will transfer to BCBS MS the lesser amount of litigation or settlement proceeds, plus Attorney Fees. For example, if BCBS MS has reasonably incurred \$100,000 in Attorney Fees, and the Plan receives \$50,000,000 in litigation proceeds, the Plan will make a Repayment to BCBS MS totaling \$50,100,000.

15. The Department notes that if the Plan receives any restitution that is tied to the conduct underlying the Claims but was ordered pursuant to a proceeding or directive that is external to Case number 20-CIV-07606, the disposition of such proceeds must conform to the requirements of this exemption.

16. BCBS MS retained Gallagher Fiduciary Advisors, LLC (Gallagher or the Independent Fiduciary) of New York, New York, to serve as the Plan's independent fiduciary with respect to the Required Restorative Payments and the potential repayment by the Plan of those Payments (collectively, the Proposed Transactions). Gallagher represents that it has extensive experience in institutional investment consulting and fiduciary decision-making regarding traditional and alternative investments. Gallagher further represents that its independent fiduciary decision-making work involves acting as a fiduciary advisor or decision-maker for plans and other ERISA-regulated asset pools and that it has experience with a wide range of asset classes and litigation claims.

17. Gallagher represents that it understands its duties and responsibilities under ERISA in acting as a fiduciary on behalf of the Plan. Gallagher also acknowledges that it is authorized to take all appropriate actions to safeguard the Plan's interests, and that it will monitor the Proposed Transactions on the Plan's behalf on a continuous basis and throughout the term required by this exemption.

18. Gallagher represents that it does not have any prior relationship with any parties in interest to the Plan, including BCBS MS and any BCBS MS affiliates. Gallagher further represents the total revenues it has

received from the Plan and from parties in interest to the Plan in connection with its engagement as Independent Fiduciary represents approximately 0.78% of Gallagher's total revenue.

19. Gallagher represents that no party associated with this exemption application has or will indemnify it, in whole or in part, for negligence of any kind and/or any violation of state or federal law that may be attributable to Gallagher's performance of its duties as Independent Fiduciary to the Plan with respect to the Proposed Transactions. In addition, no contract or instrument entered into by Gallagher as Independent Fiduciary may purport to waive any liability under state or federal law for any such violation.

20. On September 17, 2020, Gallagher completed an Independent Fiduciary Report (the Independent Fiduciary Report) finding that the massive losses caused by the Trust's investment in the Allianz Structured Alpha Strategy resulted in a significant reduction to the Plan's total assets and funding level. Gallagher represents that the Required Restorative Payments, which will be received by the Plan substantially in advance of a final resolution of the Claims against Allianz and Aon, should restore the Plan's funded percentage to its pre-loss funded percentage as of January 1, 2019. The restoration of the Plan's

funding status will secure ongoing benefit payments to participants and beneficiaries.

Gallagher notes that the Contribution and Assignment Agreement provides that the Trust must reimburse BCBS MS only up to the Required Restorative Payment Amount received by the Plan, plus any reasonable legal expense paid to non-BCBS MS-related parties that were incurred by, or allocated to, BCBS MS as a result of the Claims.<sup>64</sup> Thus, if the Plan's ultimate recovery amount from the Claims is less than the Required Restorative Payment Amount, plus related litigation expenses that were allocated to the Plan, BCBS MS, not the Plan, will suffer the loss.

Gallagher states that the Proposed Transactions and the terms of the Contribution and Assignment Agreement were negotiated and approved by Gallagher in its role as the Plan's Independent Fiduciary. Gallagher states that it approved the Proposed Transactions only after conducting an extensive analysis of the damages suffered by the Plan as a result of the failed Allianz Structured Alpha Strategy. Gallagher represents that it conducted numerous discussions with Trust representatives and counsel, along with the Plan's representatives and counsel to ensure that the

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<sup>64</sup> Currently, legal fees and expenses associated with the Claims are being paid by most of the Participating Plan's trusts on a pro rata basis according to each Participating Plan's total invested assets held in the Master Trust's Allianz Structured Alpha Strategy before the losses were incurred in the first quarter 2020. The Applicant represents that the Committee reviews and approves these legal fees before passing them through to each Participating Plan.

interests of the Plan's participants and beneficiaries were protected with respect to all aspects of the Proposed Transactions. Based upon its assessment, Gallagher approved the Plan's receipt of the Required Restorative Payments from BCBS MS in exchange for the Assignment.

#### ERISA Analysis

21. Absent an exemption, the Plan's receipt of the Restorative Payments from BCBS MS in exchange for the Plan's transfer of litigation or settlement proceeds to BCBS MS would violate ERISA. In this regard, ERISA Section 406(a)(1)(A) prohibits a plan fiduciary from causing the plan to engage in a transaction if the fiduciary knows or should know that such transaction constitutes a direct or indirect sale or exchange of any property between a plan and a party in interest. BCBS MS, as an employer whose employees are covered by the Plan, is a party in interest with respect to the Plan under ERISA Section 3(14)(C). The Required Restorative Payments to the Plan and the Plan's potential repayment to BCBS MS with litigation or settlement proceeds would constitute impermissible exchanges between the Plan and a party-in-interest (BCBS MS) in violation of ERISA Section 406(a)(1)(A).

ERISA Section 406(a)(1)(B) prohibits the lending of money or other extension of credit between a plan and a party-in-interest. BCBS MS's promise to make Required

Restorative Payments to the Plan, over time, constitutes an impermissible extension of credit between the Plan and a party-in-interest in violation of ERISA Section 406(a) (1) (B) .

ERISA Section 406(a) (1) (D) prohibits a plan fiduciary from causing a plan to engage in a transaction if the fiduciary knows or should know that the transaction constitutes a direct or indirect transfer to, or use by or for the benefit of, a party-in-interest, of the income or assets of the plan. The transfer of Plan assets to BCBS MS in connection with the Repayment would constitute an impermissible transfer of Plan assets to a party-in-interest in violation of ERISA Section 406(a) (1) (D) .

#### Conditions

22. This proposed exemption contains a number of conditions that must be met. For example, the proposed exemption mandates that the Independent Fiduciary, in full accordance with its obligations of prudence and loyalty under ERISA Section 404(a) (1) (A) and (B) must:

(a) review, negotiate, and approve the terms and conditions of the Required Restorative Payments, the Repayment, and the Contribution and Assignment Agreement, before the Plan enters into such payments and the agreement;

(b) determine that the terms and conditions of the Required Restorative Payments, the Repayment, and the

Contribution and Assignment Agreement are prudent, in the interest of the Plan and its participants and beneficiaries, and protective of the rights of the Plan's participants and beneficiaries;

(c) confirm that the Required Restorative Payments are fully and timely made;

(d) monitor the Claims and confirm that the Plan receives its proper share of any litigation or settlement proceeds received by the Trust in connection with the Claims;

(e) ensure that any Repayment by the Plan to BCBS MS fully complies with the terms of this exemption and is for no more than the lesser of the total Restorative Payments actually made to the Plan by BCBS MS or the amount the Plan received from the Claims, plus Attorney Fees;

(f) ensure that any Repayment by the Plan to BCBS MS for legal expenses in connection with the Claims is limited to only reasonable legal expenses that were paid by BCBS MS to unrelated third parties for representation of the Plan and its interests (as opposed to representation of BCBS MS or the interests of any party other than the Plan) where BCBS MS was not otherwise reimbursed from a non-Plan party;

(g) monitor the Plan's Assigned Interests on an ongoing basis to determine and confirm that any excess recovery amount from the Claims (i.e., any amount that



exceeds the Required Restorative Payment Amount) is retained by the Plan;

(h) ensure that all of the conditions and definitions of this proposed exemption are met; and

(i) represent that it has not and will not enter into any agreement or instrument that violates ERISA Section 410 or Department Regulations codified at 29 CFR section 2509.75-4.<sup>65</sup>

23. This proposed exemption also requires Gallagher to respond in writing to any information requests from the Department regarding Gallagher's activities as the Plan's Independent Fiduciary. Additionally, no later than 90 days after the resolution of the litigation, Gallagher must submit a written report to the Department demonstrating that all terms and conditions of the exemption have been met.

24. This proposed exemption requires that the Plan has not and will not release any claims, demands and/or causes of action it may have against: (a) any fiduciary of the Plan; (b) any fiduciary of the Trust; (c) BCBS MS; and/or (d) any person or entity related to a person or entity described in (a)-(c) of this paragraph. Additionally, any Repayment by the Plan to BCBS MS must be

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<sup>65</sup> ERISA Section 410 provides, in part, that "except as provided in ERISA Sections 405(b)(1) and 405(d), any provision in an agreement or instrument which purports to relieve a fiduciary from responsibility or liability for any responsibility, obligation, or duty under this part [meaning Part 4 of Title I of ERISA] shall be void as against public policy."

made in a manner designed to minimize unnecessary costs and disruption to the Plan and its investments.

25. The Plan may not make any Repayment to BCBS MS before the date: the Plan has received from BCBS MS the entire amount of the Restorative Payments agreed to in the Amended Contribution and Assignment Agreement; and all the Claims are settled. Furthermore, the Plan may not pay any interest to BCBS MS in connection with its receipt of the Required Restorative Payments, nor pledge Plan assets to secure any portion of the Required Restorative Payments.

26. Pursuant to this proposed exemption, the Plan may not incur any expenses, commissions or transaction costs in connection with the Proposed Transactions. However, as noted above, under certain circumstances the Plan may reimburse BCBS MS for reasonable legal expenses arising from the Claims that BCBS MS paid to non-BCBS MS-related parties for representation of the Plan and its interests (as opposed to representation of BCBS MS or the interests of any party other than the Plan) where BCBS MS was not otherwise reimbursed by a non-Plan party.

27. Finally, the exemptive relief provided under this proposed exemption is conditioned upon the Department's assumption that the material facts and representations set forth above in the Summary of Facts and Representation section are true and accurate at all times. In the event that a material fact or representation detailed above is

untrue or inaccurate, the exemptive relief provided under this exemption will cease immediately.

### Statutory Findings

28. ERISA Section 408(a) provides, in part, that the Department may not grant an exemption unless the Department finds that the exemption is administratively feasible, in the interest of affected plans and of their participants and beneficiaries, and protective of the rights of such participants and beneficiaries. Each of these criteria is discussed below.

a. The Proposed Exemption Is "Administratively Feasible." The Department has tentatively determined that the proposed exemption is administratively feasible because, among other things, the Independent Fiduciary will represent the interests of the Plan for all purposes with respect to the Proposed Transactions.<sup>66</sup> In this regard, not later than 90 days after the resolution of the litigation, the Independent Fiduciary must submit a written report to the Department demonstrating that all of the requirements of this exemption have been met.

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<sup>66</sup> This proposed exemption would require that if the Independent Fiduciary resigns, is removed, or for any reason is unable to serve as an Independent Fiduciary, the successor Independent Fiduciary must, among other things, assume all of the duties of the outgoing Independent Fiduciary. As soon as possible, including before the appointment of a successor Independent Fiduciary, the Plan Sponsor and the Plan must notify the Department's Office of Exemption Determinations of the change in Independent Fiduciaries. The notification must contain all material information including the qualifications of the successor Independent Fiduciary.

b. The Proposed Exemption Is "In the Interests of the Plan." The Department has tentatively determined that the proposed exemption is in the interest of the Plan because, among other things, the Plan's receipt of the Required Restorative Payments substantially improved the Plan's funding status, which enhanced the Plan's ability to meet its obligations to fund benefit obligations to participants and beneficiaries and helped the Plan avoid the imposition of benefit limitations imposed under Code section 436.

c. The Proposed Exemption Is "Protective of the Plan." The Department has tentatively determined that the proposed exemption is protective of the rights of the Plan's participants and beneficiaries because, among other things, the Plan will repay BCBS MS the lesser of the Required Restorative Payment Amount received by the Plan, or the amount the Plan receives in proceeds from the Claims, ensuring that the Proposed Transactions will result in an increase in Plan assets of at least the total amount of Restorative Payments (less reasonable legal expenses related to the Claims paid by BCBS MS to unrelated third parties, as confirmed and approved by the Independent Fiduciary). Further, this exemption preserves any right, claim, demand and/or cause of action the Plan may have against: (a) any fiduciary of the Plan; (b) any fiduciary of the Trust; (c) BCBS MS; and/or (d) any person or entity related to a person or entity described in (a)-(c).

### Summary

29. Based on the conditions described above, the Department has tentatively determined that the relief sought by the Applicant satisfies the statutory requirements under ERISA Section 408(a) for the Department to make findings that support its issuance of a proposed exemption.

### **PROPOSED EXEMPTION**

The Department is considering granting an exemption under the authority of ERISA Section 408(a) and Code Section 4975(c)(2) and in accordance with the procedures set forth in the Department's exemption procedure regulation.<sup>67</sup>

#### **Section I. Definitions**

(a) The term "Attorney Fees" means reasonable legal expenses paid by BCBS MS on behalf of the Plan in connection with the Claims, if such fees are reviewed and approved by a qualified independent fiduciary who confirms that the fees were reasonably incurred and paid by BCBS MS to unrelated third parties. For the purposes of this exemption, the Attorney Fees reimbursable to BCBS MS do not include: (1) legal expenses paid by the Plan; and (2) legal

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<sup>67</sup> 29 CFR part 2570, subpart B (55 FR 32836, 32847, August 10, 1990).

expenses paid by BCBS MS for representation of BCBS MS or the interests of any party other than the Plan.

(b) The term "BCBS MS" means Blue Cross and Blue Shield of Mississippi, a Mutual Insurance Company.

(c) The term "Claims" means the legal claims against Allianz Global Investors U.S. LLC (Allianz) and Aon Investments USA Inc. (Aon), to recover certain losses incurred by the Plan in the first quarter of 2020.

(d) The term "Contribution and Assignment Agreement" means the written agreement between BCBS MS and the Plan, dated September 17, 2020, containing all material terms regarding BCBS MS's agreement to make Required Restorative Payments to the Plan in return for the Plan's potential Repayment to BCBS MS of an amount that is no more than lesser of the Required Restorative Payment Amount (as described in Section I(h)) or the amount of litigation proceeds the Plan receives from the Claims, plus reasonable attorney fees paid to unrelated third parties by BCBS MS in connection with the Claims.

(e) The term "Independent Fiduciary" means Gallagher Fiduciary Advisors, LLC (Gallagher) or a successor Independent Fiduciary to the extent Gallagher or the successor Independent Fiduciary continues to serve in such capacity who:

(1) Is not an affiliate of BCBS MS and does not hold an ownership interest in BCBS MS or affiliates of BCBS MS;

(2) Was not a fiduciary with respect to the Plan before its appointment to serve as the Independent Fiduciary;

(3) Has acknowledged in writing that it:

(i) is a fiduciary with respect to the Plan and has agreed not to participate in any decision regarding any transaction in which it has an interest that might affect its best judgment as a fiduciary; and

(ii) Has appropriate technical training or experience to perform the services contemplated by the exemption;

(4) Has not entered into any agreement or instrument that violates the prohibitions on exculpatory provisions in ERISA Section 410 or the Department's regulation relating to indemnification of fiduciaries;<sup>68</sup>

(5) Has not received gross income from BCBS MS or its affiliates during any fiscal year in an amount that exceeds two percent (2%) of the Independent Fiduciary's gross income from all sources for the prior fiscal year. This provision also applies to a partnership or corporation of which the Independent Fiduciary is an officer, director, or 10 percent (10%) or more partner or shareholder, and

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<sup>68</sup> 29 CFR 2509.75-4.

includes as gross income amounts received as compensation for services provided as an independent fiduciary under any prohibited transaction exemption granted by the Department; and

(6) No organization or individual that is an Independent Fiduciary, and no partnership or corporation of which such organization or individual is an officer, director, or ten percent (10%) or more partner or shareholder, may acquire any property from, sell any property to, or borrow any funds from BCBS MS or from affiliates of BCBS MS while serving as an Independent Fiduciary. This prohibition will continue for six months after the party ceases to be an Independent Fiduciary and/or the Independent Fiduciary negotiates any transaction on behalf of the Plan during the period that the organization or individual serves as an Independent Fiduciary.

(f) The "Plan" means the Non-Contributory Retirement Program for Certain Employees of Blue Cross and Blue Shield of Mississippi.

(g) The term "Plan Losses" means the \$102,446,155 in Plan losses the BCBSA's National Employee Benefits Committee alleges were the result of breaches of fiduciary responsibilities and breaches of contract by Allianz Global Investors U.S. LLC and/or Aon Investments USA Inc.



(h) The term "Restorative Payments" means the payments made by BCBS MS to the Plan in connection with the Plan Losses, defined above, consisting of: (1) the past payment of \$70,000,000 made on September 21, 2020; and (2) the past payment of \$12,000,000 made on November 25, 2020. The sum of (1) and (2) is the Required Restorative Payment Amount.

(i) The "Repayment" means the payment, if any, that the Plan will transfer to BCBS MS following the Plan's receipt of proceeds from the Claims, where the Repayment is made following the full and complete resolution of the Claims; and in a manner that is consistent with the terms of the exemption.

## **Section II. Proposed Transactions**

If the proposed exemption is granted, the restrictions of ERISA Sections 406(a)(1)(A), (B) and (D) and the sanctions resulting from the application of Code Section 4975, by reason of Code Sections 4975(c)(1)(A), (B) and (D), shall not apply, effective September 17, 2020, to the following transactions: BCBS MS's transfer of Restorative Payments to the Plan; and, in return, the Plan's Repayment of an amount to BCBS MS, which must be no more than the lesser of the Restorative Payments or the amount of litigation proceeds the Plan received from the Claims, plus reasonable Attorney Fees, provided that the Definitions set forth in Section I and the Conditions set forth in Section III are met.

### **Section III. Conditions**

(a) The Plan received the entire Restorative Payment Amount no later than November 25, 2020;

(b) In connection with its receipt of the Required Restorative Payments, the Plan does not release any claims, demands and/or causes of action the Plan may have against the following: (1) any fiduciary of the Plan; (2) any fiduciary of the Trust; (3) BCBS MS; and/or (4) any person or entity related to a person or entity identified in (1)-(3) of this paragraph;

(c) The Plan's Repayment to BCBS MS is for no more than the lesser of the total Restorative Payments received by the Plan or the amount of litigation proceeds the Plan receives from the Claims. The Plan's Repayment to BCBS MS may only occur after the Independent Fiduciary has determined that: all the conditions of the exemption are met; the Plan has received all the Restorative Payments it is due; and the Plan has received all the litigation proceeds it is due. The Plan's Repayment to BCBS MS must be carried out in a manner designed to minimize unnecessary costs and disruption to the Plan and its investments;

(d) A qualified independent fiduciary (the Independent Fiduciary, as further defined in Section II(e)), acting solely on behalf of the Plan in full accordance with its

obligations of prudence and loyalty under ERISA Sections 404(a)(1)(A) and (B) must:

(1) Review, negotiate and approve the terms and conditions of the Restorative Payments and the Repayment and the Contribution and Assignment Agreement, all of which must be in writing, before the Plan enters into those transactions/agreement;

(2) Determine that the Restorative Payments, the Repayment, and the terms of the Contribution and Assignment Agreement, are prudent and in the interest of the Plan and its participants and beneficiaries;

(3) Confirm that the Required Restorative Payments were fully and timely made;

(4) Monitor the litigation related to the Claims and confirm that the Plan receives, in a timely manner, its proper share of any litigation or settlement proceeds received by the Trust;

(5) Ensure that any Repayment by the Plan to BCBS MS for legal expenses in connection with the Claims is limited to only reasonable legal expenses that were paid by BCBS MS to unrelated third parties;

(6) Ensure that all of the conditions and definitions of this proposed exemption are met;

(7) Submit a written report to the Department's Office of Exemption Determinations demonstrating and

confirming that the terms and conditions of the exemption were met, within 90 days after the Repayment; and

(8) Not enter into any agreement or instrument that violates ERISA Section 410 or the Department's Regulations codified at 29 CFR Section 2509.75-4.

(f) The Plan pays no interest in connection with the Restorative Payments;

(g) The Plan does not pledge any Plan assets to secure any portion of the Restorative Payments;

(h) The Plan does not incur any expenses, commissions, or transaction costs in connection with the Proposed Transactions. However, if first approved by the Independent Fiduciary, the Plan may reimburse BCBS MS for reasonable legal expenses paid in connection with the Claims by BCBS MS to non-BCBS MS-related parties. For purposes of determining the amount of Attorney Fees the Plan may reimburse to BCBS MS under this proposal, the amount of reasonable attorney fees paid by BCBS MS on behalf of the Plan in connection with the Claims must be reduced by the amount of legal fees received by BCBS MS in connection with the Claims from any non-Plan party (i.e., pursuant to a court award);

(i) The proposed transactions do not involve any risk of loss to either the Plan or the Plan's participants and beneficiaries;

(j) No party associated with this exemption has or will indemnify the Independent Fiduciary and the Independent Fiduciary will not request indemnification from any party, in whole or in part, for negligence and/or any violation of state or federal law that may be attributable to the Independent Fiduciary in performing its duties to the Plan with respect to the Proposed Transactions. In addition, no contract or instrument may purport to waive any liability under state or federal law for any such violation.

(k) If an Independent Fiduciary resigns, is removed, or for any reason is unable to serve as an Independent Fiduciary, the Independent Fiduciary must be replaced by a successor entity that: (1) meets the definition of Independent Fiduciary detailed above in Section II(e); and (2) otherwise meets all of the qualification, independence, prudence and diligence requirements set forth in this exemption. Further, any such successor Independent Fiduciary must assume all of the duties of the outgoing Independent Fiduciary. As soon as possible, including before the appointment of a successor Independent Fiduciary, BCBS MS must notify the Department's Office of Exemption Determinations of the change in Independent Fiduciary and such notification must contain all material information regarding the successor Independent Fiduciary,

including the successor Independent Fiduciary's qualifications; and

(1) All of the material facts and representations set forth in the Summary of Facts and Representation are true and accurate at all times.

#### NOTICE TO INTERESTED PERSONS

The Applicant will give notice of the proposed exemption to all interested persons and all of the parties to the litigation described above, within fifteen calendar days after the publication of the notice of proposed exemption in the *Federal Register*. The notice will contain a copy of the notice of proposed exemption, as published in the *Federal Register*, and a supplemental statement, as required pursuant to the Department's regulations codified at 29 CFR 2570.43(a)(2). The supplemental statement will inform interested persons of their right to comment on the pending exemption. Written comments are due by [INSERT DATE THAT IS 45 DAYS FROM THE PUBLICATION OF THE NOTICE IN THE *FEDERAL REGISTER*].

All comments will be made available to the public.

**Warning:** If you submit a comment, EBSA recommends that you include your name and other contact information in the body of your comment, but DO NOT submit information that you consider to be confidential, or otherwise protected (such as a Social Security number or an unlisted phone number) or

confidential business information that you do not want publicly disclosed. All comments may be posted on the Internet and can be retrieved by most Internet search engines.

*For Further Information Contact:* Mrs. Blessed Chuksorji-Keefe of the Department, telephone (202) 693-8567. (This is not a toll-free number.)

**Blue Cross and Blue Shield of Nebraska, Inc.**

**Located in Omaha, Nebraska**

**[Application No. D-12041]**

### **Proposed Exemption**

The Department is considering granting an exemption under the authority of Section 408(a) of the Employee Retirement Income Security Act of 1974, as amended (ERISA), and Section 4975(c)(2) of the Internal Revenue Code of 1986, as amended (the Code). The proposed exemption relates to legal actions and claims (the Claims) against Allianz Global Investors U.S. LLC (Allianz) and Aon Investments USA Inc. (Aon), that arose from certain losses incurred by the Non-Contributory Retirement Program for Certain Employees of Blue Cross and Blue Shield of Nebraska, Inc. (the Plan) in the first quarter of 2020.<sup>69</sup>

This proposed exemption would permit the past payments of \$7,000,000 and \$6,600,000 by the Plan sponsor, Blue Cross and Blue Shield of Nebraska, Inc. (BCBS Nebraska or

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<sup>69</sup> In proposing this exemption, the Department is not expressing an opinion regarding the merits of any Claim against Allianz and Aon, or whether the Plan's fiduciaries met their fiduciary duties with respect to Plan assets that are the subject of the Claims. Further, in proposing this exemption, the Department is not limiting any party's claim, demand and/or cause of action arising from the Plan's 2020 first quarter losses in any way. Among other things, this exemption preserves any right, claim, demand and/or cause of action the Plan may have against the following: (1) any fiduciary of the Plan; (2) any fiduciary of the Trust; (3) Blue Cross and Blue Shield of Nebraska, Inc.; and/or (4) any person or entity related to a person or entity described in (1)-(3).



the Applicant), to the Plan (the Restorative Payments). If the Plan receives litigation proceeds from the Claims, the Plan will transfer the lesser of the litigation proceeds amount or the Restorative Payments, plus reasonable attorney fees to BCBS Nebraska.

### **SUMMARY OF FACTS AND REPRESENTATIONS<sup>70</sup>**

1. BCBS Nebraska is a not-for-profit company that provides health insurance products and services. BCBS Nebraska is an independent licensee of the Blue Cross Blue Shield Association (BCBSA).

2. The Plan is an ERISA-covered qualified defined benefit pension plan that covers eligible employees of BCBS Nebraska. The Plan was amended, effective January 1, 2006, to close participation to new entrants as of December 31, 2005. As of August 31, 2020, the Plan covered 418 participants and held \$36,863,722 in total assets.

3. The Plan holds a beneficial interest in the Blue Cross and Blue Shield National Retirement Trust (the Trust). The Trust is a master trust that holds the assets

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<sup>70</sup> The Department notes that availability of this exemption is subject to the express condition that the material facts and representations contained in application D-12041 are true and complete at all times and accurately describe all material terms of the transactions covered by the exemption. If there is any material change in a transaction covered by the exemption or in a material fact or representation described in the application, the exemption will cease to apply as of the date of such change. The Summary of Facts and Representations is based on the Applicant's representations, as well as factual representations contained in the Claims' cause of action (as described below) and does not reflect factual findings or opinions of the Department, unless indicated otherwise.

of 16 defined benefit pension plans that participate in the BCBSA's National Retirement Program (the Participating Plans). Northern Trust serves as Trustee and asset custodian to the Trust and maintains separate records that reflect the net asset value of each Participating Plan. The Trust's earnings, market adjustments, and administrative expenses are allocated among the Participating Plans based on the respective Participating Plan's share of the Trust's assets. A Participating Plan's interest in the Trust's net assets is based on its share of the Trust.

4. The Committee serves as named fiduciary and administrator for each Participating Plan. The Committee is a standing committee of the BCBSA's board of directors. In 2011, the Committee invested a portion of the Trust's assets in funds managed by Allianz Global Investors U.S. LLC (Allianz), as part of a Structured Alpha Investment Strategy. These funds included: (a) AllianzGI Structured Alpha Multi-Beta Series LLC I; (b) AllianzGI Structured Alpha Emerging Markets Equity 350 LLC; and (c) AllianzGI Structured Alpha 1000 LLC (collectively, the Structured Alpha Funds).

5. The Applicant represents that the Allianz Structured Alpha strategy consisted of alpha and beta components. According to the applicant, the alpha component was an options trading strategy that Allianz

claimed would seek targeted positive return potential while maintaining structural risk protections. The beta component was intended to provide broad market exposure to a particular asset class through investments in financial products similar to an exchange-traded fund that replicates the performance of a market index, such as the S&P 500. According to the Applicant, Allianz represented that the Structured Alpha Strategy would capitalize on the return-generating features of option selling (short volatility) while simultaneously benefitting from the risk-control attributes associated with option buying (long volatility). According to the Applicant, Allianz represented further that the alpha component would include position hedging consisting of long-volatility positions designed to protect the portfolio in the event of a market crash.

6. As of December 31, 2019, the total market value of the Plan's portion of the Trust's investment in the Allianz Structured Alpha Funds was \$42,147,684, which represented 59.39% of total Plan assets.<sup>71</sup>

7. In 2009, the Committee retained Aon (then called Ennis Knupp) to provide investment advice regarding the investment of Plan assets held in the Trust. The Applicant represents that Aon provided regular investment advice pursuant to a written contract between it and the

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<sup>71</sup> By proposing this exemption, the Department does not, in any way, suggest a conclusion that the Plan's fiduciaries met their ERISA Section 404 duties when they caused the Trust to invest 59.39% of the Plan's total assets in the Allianz Structured Alpha Funds.

Committee. Pursuant to its engagement, Aon agreed to provide the following: "recommendations to [the Committee] regarding asset allocation" within the Trust; "recommendations to [the Committee] regarding the specific asset allocation and other investment guidelines" for the Trust's investment managers such as Allianz; and advice "regarding the diversification of assets" held in the Trust." The Applicant represents that Aon agreed to: conduct "active, ongoing monitoring" of Allianz to "identify any forward-looking" risks "that could impact performance;" and "inform itself" of any information necessary to discharge its duty to monitor, including information about the actual options positions Allianz had constructed.

8. The Applicant represents that when equity markets sharply declined in February and March of 2020, volatility spiked and the options positions held within the Structured Alpha Strategy were exposed to a heightened risk of loss. The Applicant represents that, unbeknownst to the Committee, and in violation of Allianz's stated investment strategy, Allianz abandoned the hedging strategy that was the supposed cornerstone of the Structured Alpha Strategy, leaving the portfolio almost entirely unhedged against a spike in market volatility. As described in the Claims, although Allianz had represented that it would buy hedges at strike prices ranging from 10% to 25% below the market,

the hedges it actually held at the end of February 2020 were as much as 60% below the market.

The Applicant represents that, as of January 31, 2020, the Trust had invested approximately \$2,916,049,486 in the Structured Alpha Strategy. Six weeks later, the Trust faced a margin call, which the Applicant states left it no choice but to liquidate the investment. The Trust was ultimately able to redeem only \$646,762,678 of its \$2,916,049,486 investment, resulting in a total loss of \$2,269,286,808.

Specifically, regarding the Plan's portion of the loss, as of December 31, 2019 the market value of Plan assets was \$70,967,280. As of March 31, 2020, the market value of Plan assets decreased to \$36,028,581. The Applicant represents that the Plan's total losses from the Allianz Structured Alpha Strategy were \$33,649,481, which caused the Plan to be underfunded.

9. On September 16, 2020, the Committee filed a cause of action in the United States District Court for the Southern District of New York (Case number 20-CIV-07606) against Allianz and Aon for Breach of Fiduciary Duty under ERISA Section 404, Breach of Co-Fiduciary Duty under ERISA Section 405, and violation of ERISA Section 406(b) for managing the Plan assets in its self-interest and breach of contract. It is possible that resolution of this claim and other legal actions against Allianz and Aon in connection

with the Plan's losses (the Claims) could take an extended period of time.

10. The Applicant states that rather than wait for the Claims to be resolved, BCBS Nebraska took steps to protect Plan benefits and avoid onerous benefit restrictions under Code section 436 that could apply to the Plan as a result of a funding shortfall. Therefore, on November 5, 2020, BCBS Nebraska and the Plan entered into a Contribution and Assignment Agreement (the Contribution and Assignment Agreement). Pursuant to the Contribution and Assignment Agreement, BCBS Nebraska agreed to make Restorative Payments to the Plan not in excess of \$33,649,481 by September 15, 2022. Subsequently, on August 25, 2021, BCBS Nebraska made a \$7,000,000 Restorative Payment to the Plan.

11. On March 17, 2022, BCBS Nebraska and the Plan amended the Restorative Payments provision of the Contribution and Assignment Agreement to require BCBS Nebraska to make one additional Restorative Payment of \$6,600,000 to the Plan by September 15, 2022. Subsequently, on March 29, 2022, BCBS Nebraska made a \$6,600,000 Restorative Payment to the Plan.

12. In exchange for the Restorative Payments, the Plan assigned to BCBS Nebraska its right to retain certain litigation and/or settlement proceeds recovered from the

Claims (the Assigned Interests).<sup>72</sup> Per the assignment, once the Allianz/Aon litigation is resolved and if the Plan receives litigation proceeds from the Claims, the Plan will transfer to BCBS Nebraska a repayment (the Repayment) that does not exceed the total Restorative Payments made by BCBS Nebraska as of that date, plus reasonable attorney fees paid by BCBS Nebraska on behalf of the Plan in connection with the Claims, if such fees are reviewed and approved by a qualified independent fiduciary who confirms that the fees were reasonably incurred and paid by BCBS Nebraska to unrelated third parties (the Attorney Fees).

For the purposes of this exemption, Attorney Fees reimbursable to BCBS Nebraska do not include: (a) legal expenses paid by the Plan; and (b) legal expenses paid by BCBS Nebraska for representation of its own interests or the interests of any party other than the Plan. For purposes of determining the amount of Attorney Fees the Plan may reimburse to BCBS Nebraska under this exemption, the amount of reasonable attorney fees paid by BCBS Nebraska on behalf of the Plan in connection with the Claims must be reduced by the amount of legal fees received by BCBS Nebraska in connection with the Claims from any

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<sup>72</sup> Under the Contribution and Assignment Agreement, if the Plan receives litigation or settlement proceeds from the Claims, the proceeds would first flow to the Trust, and then each Plan's pro rata portion of the proceeds would be deposited into the individual trust funding that Plan.

non-Plan party (for example, from a third party pursuant to a court award).

13. The Plan must ultimately receive at least the full value of the promised Restorative Payments, minus the Attorney Fees. The Plan may ultimately receive more than the Restorative Payment amount required under the Contribution and Assignment Agreement. If the Plan receives litigation or settlement proceeds that exceed the amount of Restorative Payments that BCBS Nebraska has made to the Plan, the Plan's Repayment to BCBS Nebraska will be limited to the amount of Restorative Payments actually made by BCBS Nebraska, plus Attorney Fees. For example, if BCBS Nebraska has reasonably incurred \$100,000 in Attorney Fees, and the Plan receives \$30,000,000 in litigation proceeds, the Plan will make a Repayment to BCBS Nebraska totaling \$13,700,000.

14. Alternatively, if the Plan receives less litigation or settlement proceeds than the amount of Restorative Payments that BCBS Nebraska has made to the Plan, the Plan will transfer to BCBS Nebraska the lesser amount of litigation or settlement proceeds, plus Attorney Fees. For example, if BCBS Nebraska reasonably incurred \$100,000 in Attorney Fees, and the Plan receives \$5,000,000 in litigation proceeds, the Plan will make a Repayment to BCBS Nebraska totaling \$5,100,000.



15. The Department notes that if the Plan receives any restitution that is tied to the conduct underlying the Claims but was ordered pursuant to a proceeding or directive that is external to Case number 20-CIV-07606, the disposition of such proceeds must conform to the requirements of this exemption.

16. BCBS Nebraska retained Gallagher Fiduciary Advisors, LLC (Gallagher or the Independent Fiduciary) of New York, New York, to serve as the Plan's independent fiduciary with respect to the Required Restorative Payments and the potential repayment by the Plan of those Payments (collectively, the Proposed Transactions). Gallagher represents that it has extensive experience in institutional investment consulting and fiduciary decision-making regarding traditional and alternative investments. Gallagher further represents that its independent fiduciary decision-making work involves acting as a fiduciary advisor or decision-maker for plans and other ERISA-regulated asset pools and that it has experience with a wide range of asset classes and litigation claims.

17. Gallagher represents that it understands its duties and responsibilities under ERISA in acting as a fiduciary on behalf of the Plan. Gallagher also acknowledges that it is authorized to take all appropriate actions to safeguard the Plan's interests, and that it will monitor the Proposed Transactions on the Plan's behalf on a

continuous basis and throughout the term required by this exemption.

18. Gallagher represents that it does not have any prior relationship with any parties in interest to the Plan, including BCBS Nebraska and any BCBS Nebraska affiliates. Gallagher further represents the total revenues it has received from the Plan and from parties in interest to the Plan in connection with its engagement as Independent Fiduciary represents approximately 0.78% of Gallagher's total revenue.

19. Gallagher represents that no party associated with this exemption application has or will indemnify it, in whole or in part, for negligence of any kind and/or any violation of state or federal law that may be attributable to Gallagher's performance of its duties as Independent Fiduciary to the Plan with respect to the Proposed Transactions. In addition, no contract or instrument entered into by Gallagher as Independent Fiduciary may purport to waive any liability under state or federal law for any such violation.

20. On November 5, 2020, Gallagher completed an Independent Fiduciary Report (the Independent Fiduciary Report) finding that the massive losses caused by the Trust's investment in the Allianz Structured Alpha Strategy resulted in a significant reduction to the Plan's total assets and funding level. Gallagher represents that the

Required Restorative Payments, which will be received by the Plan substantially in advance of a final resolution of the Claims against Allianz and Aon, should restore the Plan's funded percentage to its pre-loss funded percentage as of January 1, 2019. The restoration of the Plan's funding status will secure ongoing benefit payments to participants and beneficiaries.

Gallagher notes that the Contribution and Assignment Agreement provides that the Trust must reimburse BCBS Nebraska only up to the Required Restorative Payment Amount received by the Plan, plus any reasonable legal expense paid to non-BCBS Nebraska-related parties that were incurred by, or allocated to, BCBS Nebraska as a result of the Claims.<sup>73</sup> Thus, if the Plan's ultimate recovery amount from the Claims is less than the Required Restorative Payment Amount, plus related litigation expenses that were allocated to the Plan, BCBS Nebraska, not the Plan, will suffer the loss.

Gallagher states that the Proposed Transactions and the terms of the Contribution and Assignment Agreement were negotiated and approved by Gallagher in its role as the Plan's Independent Fiduciary. Gallagher states that it

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<sup>73</sup> Currently, legal fees and expenses associated with the Claims are being paid by most of the Participating Plan's trusts on a pro rata basis according to each Participating Plan's total invested assets held in the Master Trust's Allianz Structured Alpha Strategy before the losses were incurred in the first quarter 2020. The Applicant represents that the Committee reviews and approves these legal fees before passing them through to each Participating Plan.

approved the Proposed Transactions only after conducting an extensive analysis of the damages suffered by the Plan as a result of the failed Allianz Structured Alpha Strategy. Gallagher represents that it conducted numerous discussions with Trust representatives and counsel, along with the Plan's representatives and counsel to ensure that the interests of the Plan's participants and beneficiaries were protected with respect to all aspects of the Proposed Transactions. Based upon its assessment, Gallagher approved the Plan's receipt of the Required Restorative Payments from BCBS Nebraska in exchange for the Assignment.

#### ERISA Analysis

21. Absent an exemption, the Plan's receipt of the Restorative Payments from BCBS Nebraska in exchange for the Plan's transfer of litigation or settlement proceeds to BCBS Nebraska would violate ERISA. In this regard, ERISA Section 406(a)(1)(A) prohibits a plan fiduciary from causing the plan to engage in a transaction if the fiduciary knows or should know that such transaction constitutes a direct or indirect sale or exchange of any property between a plan and a party in interest. BCBS Nebraska, as an employer whose employees are covered by the Plan, is a party in interest with respect to the Plan under ERISA Section 3(14)(C). The Required Restorative Payments to the Plan and the Plan's potential repayment to BCBS

Nebraska with litigation or settlement proceeds would constitute impermissible exchanges between the Plan and a party-in-interest (BCBS Nebraska) in violation of ERISA Section 406(a) (1) (A) .

ERISA Section 406(a) (1) (B) prohibits the lending of money or other extension of credit between a plan and a party-in-interest. BCBS Nebraska's promise to make Required Restorative Payments to the Plan, over time, constitutes an impermissible extension of credit between the Plan and a party-in-interest in violation of ERISA Section 406(a) (1) (B) .

ERISA Section 406(a) (1) (D) prohibits a plan fiduciary from causing a plan to engage in a transaction if the fiduciary knows or should know that the transaction constitutes a direct or indirect transfer to, or use by or for the benefit of, a party-in-interest, of the income or assets of the plan. The transfer of Plan assets to BCBS Nebraska in connection with the Repayment would constitute an impermissible transfer of Plan assets to a party-in-interest in violation of ERISA Section 406(a) (1) (D) .

#### Conditions

22. This proposed exemption contains a number of conditions that must be met. For example, the proposed exemption mandates that the Independent Fiduciary, in full accordance with its obligations of prudence and loyalty under ERISA Section 404(a) (1) (A) and (B) must:

(a) review, negotiate, and approve the terms and conditions of the Required Restorative Payments, the Repayment, and the Contribution and Assignment Agreement, before the Plan enters into such payments and the agreement;

(b) determine that the terms and conditions of the Required Restorative Payments, the Repayment, and the Contribution and Assignment Agreement are prudent, in the interest of the Plan and its participants and beneficiaries, and protective of the rights of the Plan's participants and beneficiaries;

(c) confirm that the Required Restorative Payments are fully and timely made;

(d) monitor the Claims and confirm that the Plan receives its proper share of any litigation or settlement proceeds received by the Trust in connection with the Claims;

(e) ensure that any Repayment by the Plan to BCBS Nebraska fully complies with the terms of this exemption and is for no more than the lesser of the total Restorative Payments actually made to the Plan by BCBS Nebraska or the amount the Plan received from the Claims, plus Attorney Fees;

(f) ensure that any Repayment by the Plan to BCBS Nebraska for legal expenses in connection with the Claims is limited to only reasonable legal expenses that were paid

by BCBS Nebraska to unrelated third parties for representation of the Plan and its interests (as opposed to representation of BCBS Nebraska or the interests of any party other than the Plan) where BCBS Nebraska was not otherwise reimbursed from a non-Plan party;

(g) monitor the Plan's Assigned Interests on an ongoing basis to determine and confirm that any excess recovery amount from the Claims (i.e., any amount that exceeds the Required Restorative Payment Amount) is retained by the Plan;

(h) ensure that all of the conditions and definitions of this proposed exemption are met; and

(i) represent that it has not and will not enter into any agreement or instrument that violates ERISA Section 410 or Department Regulations codified at 29 CFR section 2509.75-4.<sup>74</sup>

23. This proposed exemption also requires Gallagher to respond in writing to any information requests from the Department regarding Gallagher's activities as the Plan's Independent Fiduciary. Additionally, no later than 90 days after the resolution of the litigation, Gallagher must submit a written report to the Department demonstrating

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<sup>74</sup> ERISA Section 410 provides, in part, that "except as provided in ERISA Sections 405(b)(1) and 405(d), any provision in an agreement or instrument which purports to relieve a fiduciary from responsibility or liability for any responsibility, obligation, or duty under this part [meaning Part 4 of Title I of ERISA] shall be void as against public policy."

that all terms and conditions of the exemption have been met.

24. This proposed exemption requires that the Plan has not and will not release any claims, demands and/or causes of action it may have against: (a) any fiduciary of the Plan; (b) any fiduciary of the Trust; (c) BCBS Nebraska; and/or (d) any person or entity related to a person or entity described in (a)-(c) of this paragraph. Additionally, any Repayment by the Plan to BCBS Nebraska must be made in a manner designed to minimize unnecessary costs and disruption to the Plan and its investments.

25. The Plan may not make any Repayment to BCBS Nebraska before the date: the Plan has received from BCBS Nebraska the entire amount of the Restorative Payments agreed to in the Amended Contribution and Assignment Agreement, and all the Claims are settled. Furthermore, the Plan may not pay any interest to BCBS Nebraska in connection with its receipt of the Required Restorative Payments, nor pledge Plan assets to secure any portion of the Required Restorative Payments.

26. Pursuant to this proposed exemption, the Plan may not incur any expenses, commissions or transaction costs in connection with the Proposed Transactions. However, as noted above, under certain circumstances the Plan may reimburse BCBS Nebraska for reasonable legal expenses arising from the Claims that BCBS Nebraska paid to non-BCBS



Nebraska-related parties for representation of the Plan and its interests (as opposed to representation of BCBS Nebraska or the interests of any party other than the Plan) where BCBS Nebraska was not otherwise reimbursed by a non-Plan party.

27. Finally, the exemptive relief provided under this proposed exemption is conditioned upon the Department's assumption that the material facts and representations set forth above in the Summary of Facts and Representation section are true and accurate at all times. In the event that a material fact or representation detailed above is untrue or inaccurate, the exemptive relief provided under this exemption will cease immediately.

#### Statutory Findings

28. ERISA Section 408(a) provides, in part, that the Department may not grant an exemption unless the Department finds that the exemption is administratively feasible, in the interest of affected plans and of their participants and beneficiaries, and protective of the rights of such participants and beneficiaries. Each of these criteria is discussed below.

a. The Proposed Exemption Is "Administratively Feasible." The Department has tentatively determined that the proposed exemption is administratively feasible because, among other things, the Independent Fiduciary will represent the interests of the Plan for all purposes with respect to

the Proposed Transactions.<sup>75</sup> In this regard, not later than 90 days after the resolution of the litigation, the Independent Fiduciary must submit a written report to the Department demonstrating that all of the requirements of this exemption have been met.

b. The Proposed Exemption Is "In the Interests of the Plan." The Department has tentatively determined that the proposed exemption is in the interest of the Plan because, among other things, the Plan's receipt of the Required Restorative Payments substantially improved the Plan's funding status, which enhanced the Plan's ability to meet its obligations to fund benefit obligations to participants and beneficiaries and helped the Plan avoid the imposition of benefit limitations imposed under Code section 436.

c. The Proposed Exemption Is "Protective of the Plan." The Department has tentatively determined that the proposed exemption is protective of the rights of the Plan's participants and beneficiaries because, among other things, the Plan will repay BCBS Nebraska the lesser of the Required Restorative Payment Amount received by the Plan, or the amount the Plan receives in proceeds from the Claims,

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<sup>75</sup> This proposed exemption would require that if the Independent Fiduciary resigns, is removed, or for any reason is unable to serve as an Independent Fiduciary, the successor Independent Fiduciary must, among other things, assume all of the duties of the outgoing Independent Fiduciary. As soon as possible, including before the appointment of a successor Independent Fiduciary, the Plan Sponsor and the Plan must notify the Department's Office of Exemption Determinations of the change in Independent Fiduciaries. The notification must contain all material information including the qualifications of the successor Independent Fiduciary.

ensuring that the Proposed Transactions will result in an increase in Plan assets of at least the total amount of Restorative Payments (less reasonable legal expenses related to the Claims paid by BCBS Nebraska to unrelated third parties, as confirmed and approved by the Independent Fiduciary). Further, this exemption preserves any right, claim, demand and/or cause of action the Plan may have against: (a) any fiduciary of the Plan; (b) any fiduciary of the Trust; (c) BCBS Nebraska; and/or (d) any person or entity related to a person or entity described in (a)-(c).

#### Summary

29. Based on the conditions described above, the Department has tentatively determined that the relief sought by the Applicant satisfies the statutory requirements under ERISA Section 408(a) for the Department to make findings that support its issuance of a proposed exemption.

#### **PROPOSED EXEMPTION**

The Department is considering granting an exemption under the authority of ERISA Section 408(a) and Code Section 4975(c)(2) and in accordance with the procedures set forth in the Department's exemption procedure regulation.<sup>76</sup>

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<sup>76</sup> 29 CFR part 2570, subpart B (55 FR 32836, 32847, August 10, 1990).

## **Section I. Definitions**

(a) The term "Attorney Fees" means reasonable legal expenses paid by BCBS Nebraska on behalf of the Plan in connection with the Claims, if such fees are reviewed and approved by a qualified independent fiduciary who confirms that the fees were reasonably incurred and paid by BCBS Nebraska to unrelated third parties. For the purposes of this exemption, the Attorney Fees reimbursable to BCBS Nebraska do not include: (1) legal expenses paid by the Plan; and (2) legal expenses paid by BCBS Nebraska for representation of BCBS Nebraska or the interests of any party other than the Plan.

(b) The term "BCBS Nebraska" means Blue Cross and Blue Shield of Nebraska, Inc.

(c) The term "Claims" means the legal claims against Allianz Global Investors U.S. LLC (Allianz) and Aon Investments USA Inc. (Aon), to recover certain losses incurred by the Plan in the first quarter of 2020.

(d) The term "Contribution and Assignment Agreement" means the written agreement between BCBS Nebraska and the Plan, dated November 5, 2020, and its amendment that became effective on March 17, 2022, containing all material terms regarding BCBS Nebraska's agreement to make Required Restorative Payments to the Plan in return for the Plan's potential Repayment to BCBS Nebraska of an amount that is

no more than lesser of the Required Restorative Payment Amount (as described in Section I(h)) received by the Plan or the amount of litigation proceeds the Plan receives from the Claims, plus reasonable attorney fees paid to unrelated third parties by BCBS Nebraska in connection with the Claims.

(e) The term "Independent Fiduciary" means Gallagher Fiduciary Advisors, LLC (Gallagher) or a successor Independent Fiduciary to the extent Gallagher or the successor Independent Fiduciary continues to serve in such capacity who:

(1) Is not an affiliate of BCBS Nebraska and does not hold an ownership interest in BCBS Nebraska or affiliates of BCBS Nebraska;

(2) Was not a fiduciary with respect to the Plan before its appointment to serve as the Independent Fiduciary;

(3) Has acknowledged in writing that it:

(i) is a fiduciary with respect to the Plan and has agreed not to participate in any decision regarding any transaction in which it has an interest that might affect its best judgment as a fiduciary; and

(ii) Has appropriate technical training or experience to perform the services contemplated by the exemption;

(4) Has not entered into any agreement or instrument that violates the prohibitions on exculpatory provisions in ERISA Section 410 or the Department's regulation relating to indemnification of fiduciaries;<sup>77</sup>

(5) Has not received gross income from BCBS Nebraska or its affiliates during any fiscal year in an amount that exceeds two percent (2%) of the Independent Fiduciary's gross income from all sources for the prior fiscal year. This provision also applies to a partnership or corporation of which the Independent Fiduciary is an officer, director, or 10 percent (10%) or more partner or shareholder, and includes as gross income amounts received as compensation for services provided as an independent fiduciary under any prohibited transaction exemption granted by the Department; and

(6) No organization or individual that is an Independent Fiduciary, and no partnership or corporation of which such organization or individual is an officer, director, or ten percent (10%) or more partner or shareholder, may acquire any property from, sell any property to, or borrow any funds from BCBS Nebraska or from affiliates of BCBS Nebraska while serving as an Independent Fiduciary. This prohibition will continue for six months after the party ceases to be an Independent Fiduciary and/or the Independent Fiduciary negotiates any transaction

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<sup>77</sup> 29 CFR 2509.75-4.

on behalf of the Plan during the period that the organization or individual serves as an Independent Fiduciary.

(f) The "Plan" means the Non-Contributory Retirement Program for Certain Employees of Blue Cross and Blue Shield of Nebraska, Inc.

(g) The term "Plan Losses" means the \$33,649,481 in Plan losses the BCBSA's National Employee Benefits Committee alleges were the result of breaches of fiduciary responsibilities and breaches of contract by Allianz Global Investors U.S. LLC and/or Aon Investments USA Inc.

(h) The term "Restorative Payments" means the payments made by BCBS Nebraska to the Plan in connection with the Plan Losses, defined above, consisting of: (1) the past payment of \$7,000,000 on August 25, 2021; and (2) the past payment of \$6,600,000 on March 29, 2022. The sum of (1) and (2) is the Required Restorative Payment Amount.

(i) The "Repayment" means the payment, if any, that the Plan will transfer to BCBS Nebraska following the Plan's receipt of proceeds from the Claims, where the Repayment is made following the full and complete resolution of the Claims, and in a manner that is consistent with the terms of the exemption.

## **Section II. Proposed Transactions**

If the proposed exemption is granted, the restrictions of ERISA Sections 406(a)(1)(A), (B) and (D) and the sanctions resulting from the application of Code Section 4975, by reason of Code Sections 4975(c)(1)(A), (B) and (D), shall not apply, effective November 5, 2020, to the following transactions: BCBS Nebraska's transfer of Restorative Payments to the Plan; and, in return, the Plan's Repayment of an amount to BCBS Nebraska, which must be no more than the lesser of the Restorative Payment received by the Plan or the amount of litigation proceeds the Plan received from the Claims, plus reasonable Attorney Fees, provided that the Definitions set forth in Section I and the Conditions set forth in Section III are met.

## **Section III. Conditions**

(a) The Plan received the entire Restorative Payment Amount no later than March 29, 2022;

(b) In connection with its receipt of the Required Restorative Payments, the Plan does not release any claims, demands and/or causes of action the Plan may have against the following: (1) any fiduciary of the Plan; (2) any fiduciary of the Trust; (3) BCBS Nebraska; and/or (4) any person or entity related to a person or entity identified in (1)-(3) of this paragraph;



(c) The Plan's Repayment to BCBS Nebraska is for no more than the lesser of the total Restorative Payments received by the Plan or the amount of litigation proceeds the Plan receives from the Claims. The Plan's Repayment to BCBS Nebraska may only occur after the Independent Fiduciary has determined that: all the conditions of the exemption are met; the Plan has received all the Restorative Payments it is due; and the Plan has received all the litigation proceeds it is due. The Plan's Repayment to BCBS Nebraska must be carried out in a manner designed to minimize unnecessary costs and disruption to the Plan and its investments;

(d) A qualified independent fiduciary (the Independent Fiduciary, as further defined in Section II(e)), acting solely on behalf of the Plan in full accordance with its obligations of prudence and loyalty under ERISA Sections 404(a)(1)(A) and (B) must:

(1) Review, negotiate and approve the terms and conditions of the Restorative Payments and the Repayment and the Contribution and Assignment Agreement, all of which must be in writing, before the Plan enters into those transactions/agreement;

(2) Determine that the Restorative Payments, the Repayment, and the terms of the Contribution and Assignment Agreement, are prudent and in the interest of the Plan and its participants and beneficiaries;

(3) Confirm that the Required Restorative Payment Amount was fully and timely made;

(4) Monitor the litigation related to the Claims and confirm that the Plan receives, in a timely manner, its proper share of any litigation or settlement proceeds received by the Trust;

(5) Ensure that any Repayment by the Plan to BCBS Nebraska for legal expenses in connection with the Claims is limited to only reasonable legal expenses that were paid by BCBS Nebraska to unrelated third parties;

(6) Ensure that all of the conditions and definitions of this proposed exemption are met;

(7) Submit a written report to the Department's Office of Exemption Determinations demonstrating and confirming that the terms and conditions of the exemption were met, within 90 days after the Repayment; and

(8) Not enter into any agreement or instrument that violates ERISA Section 410 or the Department's Regulations codified at 29 CFR Section 2509.75-4.

(f) The Plan pays no interest in connection with the Restorative Payments;

(g) The Plan does not pledge any Plan assets to secure any portion of the Restorative Payments;

(h) The Plan does not incur any expenses, commissions, or transaction costs in connection with the Proposed Transactions. However, if first approved by the

Independent Fiduciary, the Plan may reimburse BCBS Nebraska for reasonable legal expenses paid in connection with the Claims by BCBS Nebraska to non-BCBS Nebraska-related parties. For purposes of determining the amount of Attorney Fees the Plan may reimburse to BCBS Nebraska under this proposal, the amount of reasonable attorney fees paid by BCBS Nebraska on behalf of the Plan in connection with the Claims must be reduced by the amount of legal fees received by BCBS Nebraska in connection with the Claims from any non-Plan party (i.e., pursuant to a court award);

(i) The proposed transactions do not involve any risk of loss to either the Plan or the Plan's participants and beneficiaries;

(j) No party associated with this exemption has or will indemnify the Independent Fiduciary and the Independent Fiduciary will not request indemnification from any party, in whole or in part, for negligence and/or any violation of state or federal law that may be attributable to the Independent Fiduciary in performing its duties to the Plan with respect to the Proposed Transactions. In addition, no contract or instrument may purport to waive any liability under state or federal law for any such violation.

(k) If an Independent Fiduciary resigns, is removed, or for any reason is unable to serve as an Independent Fiduciary, the Independent Fiduciary must be replaced by a

successor entity that: (1) meets the definition of Independent Fiduciary detailed above in Section II(e); and (2) otherwise meets all of the qualification, independence, prudence and diligence requirements set forth in this exemption. Further, any such successor Independent Fiduciary must assume all of the duties of the outgoing Independent Fiduciary. As soon as possible, including before the appointment of a successor Independent Fiduciary, BCBS Nebraska must notify the Department's Office of Exemption Determinations of the change in Independent Fiduciary and such notification must contain all material information regarding the successor Independent Fiduciary, including the successor Independent Fiduciary's qualifications; and

(1) All of the material facts and representations set forth in the Summary of Facts and Representation are true and accurate at all times.

#### NOTICE TO INTERESTED PERSONS

The Applicant will give notice of the proposed exemption to all interested persons and all of the parties to the litigation described above, within fifteen calendar days after the publication of the notice of proposed exemption in the *Federal Register*. The notice will contain a copy of the notice of proposed exemption, as published in the *Federal Register*, and a supplemental statement, as

required pursuant to the Department's regulations codified at 29 CFR 2570.43(a)(2). The supplemental statement will inform interested persons of their right to comment on the pending exemption. Written comments are due by [INSERT DATE THAT IS 45 DAYS FROM THE PUBLICATION OF THE NOTICE IN THE *FEDERAL REGISTER*].

All comments will be made available to the public.

**Warning:** If you submit a comment, EBSA recommends that you include your name and other contact information in the body of your comment, but DO NOT submit information that you consider to be confidential, or otherwise protected (such as a Social Security number or an unlisted phone number) or confidential business information that you do not want publicly disclosed. All comments may be posted on the Internet and can be retrieved by most Internet search engines.

*For Further Information Contact:* Mrs. Blessed Chuksorji-Keefe of the Department, telephone (202) 693-8567. (This is not a toll-free number.)

**BlueCross BlueShield of Tennessee, Inc.**

**Located in Chattanooga, Tennessee**

**[Application No. D-12045]**

### **Proposed Exemption**

The Department is considering granting an exemption under the authority of Section 408(a) of the Employee Retirement Income Security Act of 1974, as amended (ERISA), and Section 4975(c)(2) of the Internal Revenue Code of 1986, as amended (the Code). The proposed exemption relates to legal actions and claims (the Claims) against Allianz Global Investors U.S. LLC (Allianz) and Aon Investments USA Inc. (Aon), that arose from certain losses incurred by the BlueCross BlueShield of Tennessee, Inc. Pension Plan (the Plan) in the first quarter of 2020.<sup>78</sup>

This proposed exemption would permit the past payment of \$100,000,000 to the Plan by the Plan sponsor, BlueCross BlueShield of Tennessee, Inc. (BCBS Tennessee). If the Plan receives litigation proceeds from the Claims, the Plan

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<sup>78</sup> In proposing this exemption, the Department is not expressing an opinion regarding the merits of any Claim against Allianz and Aon, or whether the Plan's fiduciaries met their fiduciary duties with respect to Plan assets that are the subject of the Claims. Further, in proposing this exemption, the Department is not limiting any party's claim, demand and/or cause of action arising from the Plan's 2020 first quarter losses in any way. Among other things, this exemption preserves any right, claim, demand and/or cause of action the Plan may have against the following: (1) any fiduciary of the Plan; (2) any fiduciary of the Trust; (3) BlueCross BlueShield of Tennessee, Inc.; and/or (4) any person or entity related to a person or entity described in (1)-(3).

will transfer the lesser of the litigation proceeds amount or the Restorative Payment, plus reasonable attorney fees to BCBS Tennessee.

#### **SUMMARY OF FACTS AND REPRESENTATIONS<sup>79</sup>**

1. BCBS Tennessee is a not-for-profit company incorporated in Tennessee with its principal office in Chattanooga, Tennessee. BCBS Tennessee issues and administers health care coverage for individuals and group health plans sponsored by Tennessee-based employers and is an independent licensee of the Blue Cross Blue Shield Association (BCBSA).

2. The Plan is an ERISA-covered, frozen defined benefit pension plan that covers eligible employees of BCBS Tennessee and employees of affiliated employers. BCBS Tennessee makes all contributions to the Plan for the exclusive benefit of participants and their beneficiaries, and to cover administrative expenses. As of August 31, 2020, the Plan covered 2,628 participants and held \$203,341,148 in total assets.

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<sup>79</sup> The Department notes that availability of this exemption is subject to the express condition that the material facts and representations contained in application D-12045 are true and complete at all times and accurately describe all material terms of the transactions covered by the exemption. If there is any material change in a transaction covered by the exemption or in a material fact or representation described in the application, the exemption will cease to apply as of the date of such change. The Summary of Facts and Representations is based on the Applicant's representations, as well as factual representations contained in the Claims' cause of action (as described below) and does not reflect factual findings or opinions of the Department, unless indicated otherwise.

3. The Plan holds a beneficial interest in the Blue Cross and Blue Shield National Retirement Trust (the Trust). The Trust is a master trust that holds the assets of 16 defined benefit pension plans that participate in the BCBSA's National Retirement Program (the Participating Plans). Northern Trust serves as Trustee and asset custodian to the Trust and maintains separate records that reflect the net asset value of each Participating Plan. The Trust's earnings, market adjustments, and administrative expenses are allocated among the Participating Plans based on the respective Participating Plan's share of the Trust's assets. A Participating Plan's interest in the Trust's net assets is based on its share of the Trust.

4. The Committee serves as named fiduciary and administrator for each Participating Plan. The Committee is a standing committee of the BCBSA's board of directors. In 2011, the Committee invested a portion of the Trust's assets in funds managed by Allianz Global Investors U.S. LLC (Allianz), as part of a Structured Alpha Investment Strategy. These funds included: (a) AllianzGI Structured Alpha Multi-Beta Series LLC I; (b) AllianzGI Structured Alpha Emerging Markets Equity 350 LLC; and (c) AllianzGI Structured Alpha 1000 LLC (collectively, the Structured Alpha Funds).



5. The Applicant represents that the Allianz Structured Alpha strategy consisted of alpha and beta components. According to the applicant, the alpha component was an options trading strategy that Allianz claimed would seek targeted positive return potential while maintaining structural risk protections. The beta component was intended to provide broad market exposure to a particular asset class through investments in financial products similar to an exchange-traded fund that replicates the performance of a market index, such as the S&P 500. According to the Applicant, Allianz represented that the Structured Alpha Strategy would capitalize on the return-generating features of option selling (short volatility) while simultaneously benefitting from the risk-control attributes associated with option buying (long volatility). According to the Applicant, Allianz represented further that the alpha component would include position hedging consisting of long-volatility positions designed to protect the portfolio in the event of a market crash.

6. As of December 31, 2019, the total market value of the Plan's portion of the Trust's investment in the Allianz Structured Alpha Funds was \$138,015,536, which represented 68.57% of total Plan assets.<sup>80</sup>

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<sup>80</sup> By proposing this exemption, the Department does not, in any way, suggest a conclusion that the Plan's fiduciaries met their ERISA Section 404 duties when they caused the Trust to invest 68.57% of the Plan's total assets in the Allianz Structured Alpha Funds.

7. In 2009, the Committee retained Aon (then called Ennis Knupp) to provide investment advice regarding the investment of Plan assets held in the Trust. The Applicant represents that Aon provided regular investment advice pursuant to a written contract between it and the Committee. Pursuant to its engagement, Aon agreed to provide the following: "recommendations to [the Committee] regarding asset allocation" within the Trust; "recommendations to [the Committee] regarding the specific asset allocation and other investment guidelines" for the Trust's investment managers such as Allianz; and advice "regarding the diversification of assets" held in the Trust." The Applicant represents that Aon agreed to: conduct "active, ongoing monitoring" of Allianz to "identify any forward-looking" risks "that could impact performance;" and "inform itself" of any information necessary to discharge its duty to monitor, including information about the actual options positions Allianz had constructed.

8. The Applicant represents that when equity markets sharply declined in February and March of 2020, volatility spiked and the options positions held within the Structured Alpha Strategy were exposed to a heightened risk of loss. The Applicant represents that, unbeknownst to the Committee, and in violation of Allianz's stated investment strategy, Allianz abandoned the hedging strategy that was

the supposed cornerstone of the Structured Alpha Strategy, leaving the portfolio almost entirely unhedged against a spike in market volatility. As described in the Claims, although Allianz had represented that it would buy hedges at strike prices ranging from 10% to 25% below the market, the hedges it actually held at the end of February 2020 were as much as 60% below the market.

The Applicant represents that, as of January 31, 2020, the Trust had invested approximately \$2,916,049,486 in the Structured Alpha Strategy. Six weeks later, the Trust faced a margin call, which the Applicant states left it no choice but to liquidate the investment. The Trust was ultimately able to redeem only \$646,762,678 of its \$2,916,049,486 investment, resulting in a total loss of \$2,269,286,808.

Specifically, regarding the Plan's portion of the loss, as of December 31, 2019, the market value of the Plan's assets was \$201,265,786. As of March 31, 2020, the market value of the Plan's assets decreased to \$103,023,619. The Applicant represents that the Plan's total losses from the Allianz Structured Alpha Strategy were \$93,576,015, which caused the Plan to be underfunded.

9. On September 16, 2020, the Committee filed a cause of action in the United States District Court for the Southern District of New York (Case number 20-CIV-07606) against Allianz and Aon for Breach of Fiduciary Duty under

ERISA Section 404, Breach of Co-Fiduciary Duty under ERISA Section 405, and violation of ERISA Section 406(b) for managing the Plan assets in its self-interest and breach of contract. It is possible that resolution of this claim and other legal actions against Allianz and Aon in connection with the Plan's losses (the Claims) could take an extended period of time.

10. The Applicant states that rather than wait for the Claims to be resolved, BCBS Tennessee took steps to protect Plan benefits and avoid onerous benefit restrictions under Code section 436 that could apply to the Plan as a result of a funding shortfall. Therefore, on October 8, 2020, BCBS Tennessee and the Plan entered into a Contribution and Assignment Agreement (the Contribution and Assignment Agreement), whereby BCBS Tennessee agreed to make a \$100,000,000 payment to the Plan within seven business days of the effective date of the Contribution and Assignment Agreement (the Restorative Payment). BCBS Tennessee remitted \$100,000,000 to the Plan on October 8, 2020.

11. In exchange for the Restorative Payment, the Plan assigned to BCBS Tennessee its right to retain certain litigation and/or settlement proceeds recovered from the Claims (the Assigned Interests).<sup>81</sup> Per the assignment, once

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<sup>81</sup> Under the Contribution and Assignment Agreement, if the Plan receives litigation or settlement proceeds from the Claims, the proceeds would first flow to the Trust, and then each Plan's pro rata portion of the

the Allianz/Aon litigation is resolved and if the Plan receives litigation proceeds from the Claims, the Plan will transfer to BCBS Tennessee a repayment (the Repayment) that does not exceed the total Restorative Payment made by BCBS Tennessee, plus reasonable attorney fees paid by BCBS Tennessee on behalf of the Plan in connection with the Claims, if such fees are reviewed and approved by a qualified independent fiduciary who confirms that the fees were reasonably incurred and paid by BCBS Tennessee to unrelated third parties (the Attorney Fees). For the purposes of this exemption, Attorney Fees reimbursable to BCBS Tennessee do not include: (a) legal expenses paid by the Plan; and (b) legal expenses paid by BCBS Tennessee for representation of its own interests or the interests of any party other than the Plan. For purposes of determining the amount of Attorney Fees the Plan may reimburse to BCBS Tennessee under this exemption, the amount of reasonable attorney fees paid by BCBS Tennessee on behalf of the Plan in connection with the Claims must be reduced by the amount of legal fees received by BCBS Tennessee in connection with the Claims from any non-Plan party (for example, from a third party pursuant to a court award).

12. The Plan must ultimately receive at least the full value of the promised Restorative Payment, minus the

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proceeds would be deposited into the individual trust funding that Plan.

Attorney Fees. The Plan, however, may ultimately receive more than the Restorative Payment amount required under the Contribution and Assignment Agreement. If the Plan receives litigation or settlement proceeds that exceed the amount of the Restorative Payment that BCBS Tennessee made to the Plan, the Plan's Repayment to BCBS Tennessee will be limited to the amount of Restorative Payment made by BCBS Tennessee, plus Attorney Fees. For example, if BCBS Tennessee has reasonably incurred \$100,000 in Attorney Fees, and the Plan receives \$120,000,000 in litigation proceeds, the Plan will make a Repayment to BCBS Tennessee totaling \$100,100,000.

13. Alternatively, if the Plan receives less litigation or settlement proceeds than the amount of the Restorative Payment that BCBS Tennessee made to the Plan, the Plan will transfer to BCBS Tennessee the lesser amount of litigation or settlement proceeds, plus Attorney Fees. For example, if BCBS Tennessee has reasonably incurred \$100,000 in Attorney Fees, and the Plan receives \$50,000,000 in litigation proceeds, the Plan will make a Repayment to BCBS Tennessee totaling \$50,100,000.

14. The Department notes that if the Plan receives any restitution that is tied to the conduct underlying the Claims but was ordered pursuant to a proceeding or directive that is external to Case number 20-CIV-07606, the

disposition of such proceeds must conform to the requirements of this exemption.

15. BCBS Tennessee retained Gallagher Fiduciary Advisors, LLC (Gallagher or the Independent Fiduciary) of New York, New York, to serve as the Plan's independent fiduciary with respect to the Required Restorative Payment and the potential repayment by the Plan of that Payment (collectively, the Proposed Transactions). Gallagher represents that it has extensive experience in institutional investment consulting and fiduciary decision-making regarding traditional and alternative investments. Gallagher further represents that its independent fiduciary decision-making work involves acting as a fiduciary advisor or decision-maker for plans and other ERISA-regulated asset pools and that it has experience with a wide range of asset classes and litigation claims.

16. Gallagher represents that it understands its duties and responsibilities under ERISA in acting as a fiduciary on behalf of the Plan. Gallagher also acknowledges that it is authorized to take all appropriate actions to safeguard the Plan's interests, and that it will monitor the Proposed Transactions on the Plan's behalf on a continuous basis and throughout the term required by this exemption.

17. Gallagher represents that it does not have any prior relationship with any parties in interest to the

Plan, including BCBS Tennessee and any BCBS Tennessee affiliates. Gallagher further represents the total revenues it has received from the Plan and from parties in interest to the Plan in connection with its engagement as Independent Fiduciary represents approximately 0.78% of Gallagher's total revenue.

18. Gallagher represents that no party associated with this exemption application has or will indemnify it, in whole or in part, for negligence of any kind and/or any violation of state or federal law that may be attributable to Gallagher's performance of its duties as Independent Fiduciary to the Plan with respect to the Proposed Transactions. In addition, no contract or instrument entered into by Gallagher as Independent Fiduciary may purport to waive any liability under state or federal law for any such violation.

19. On October 8, 2020, Gallagher completed an Independent Fiduciary Report (the Independent Fiduciary Report) finding that the massive losses caused by the Trust's investment in the Allianz Structured Alpha Strategy resulted in a significant reduction to the Plan's total assets and funding level. Gallagher represents that the Required Restorative Payment, which was received by the Plan substantially in advance of a final resolution of the Claims against Allianz and Aon, should restore the Plan's funded percentage to its pre-loss funded percentage as of



January 1, 2019. The restoration of the Plan's funding status will secure ongoing benefit payments to participants and beneficiaries.

Gallagher notes that the Contribution and Assignment Agreement provides that the Trust must reimburse BCBS Tennessee only up to the Required Restorative Payment Amount received, plus any reasonable legal expense paid to non-BCBS Tennessee-related parties that were incurred by, or allocated to, BCBS Tennessee as a result of the Claims.<sup>82</sup> Thus, if the Plan's ultimate recovery amount from the Claims is less than the Required Restorative Payment Amount, plus related litigation expenses that were allocated to the Plan, BCBS Tennessee, not the Plan, will suffer the loss.

Gallagher states that the Proposed Transactions and the terms of the Contribution and Assignment Agreement were negotiated and approved by Gallagher in its role as the Plan's Independent Fiduciary. Gallagher states that it approved the Proposed Transactions only after conducting an extensive analysis of the damages suffered by the Plan as a result of the failed Allianz Structured Alpha Strategy. Gallagher represents that it conducted numerous discussions

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<sup>82</sup> Currently, legal fees and expenses associated with the Claims are being paid by most of the Participating Plan's trusts on a pro rata basis according to each Participating Plan's total invested assets held in the Master Trust's Allianz Structured Alpha Strategy before the losses were incurred in the first quarter 2020. The Applicant represents that the Committee reviews and approves these legal fees before passing them through to each Participating Plan.

with Trust representatives and counsel, along with the Plan's representatives and counsel to ensure that the interests of the Plan's participants and beneficiaries were protected with respect to all aspects of the Proposed Transactions. Based upon its assessment, Gallagher approved the Plan's receipt of the Required Restorative Payment from BCBS Tennessee in exchange for the Assignment.

#### ERISA Analysis

20. Absent an exemption, the Plan's receipt of the Restorative Payment from BCBS Tennessee in exchange for the Plan's transfer of litigation or settlement proceeds to BCBS Tennessee would violate ERISA. In this regard, ERISA Section 406(a)(1)(A) prohibits a plan fiduciary from causing the plan to engage in a transaction if the fiduciary knows or should know that such transaction constitutes a direct or indirect sale or exchange of any property between a plan and a party in interest. BCBS Tennessee, as an employer whose employees are covered by the Plan, is a party in interest with respect to the Plan under ERISA Section 3(14)(C). The Required Restorative Payment to the Plan and the Plan's potential repayment to BCBS Tennessee with litigation or settlement proceeds would constitute impermissible exchanges between the Plan and a party-in-interest (BCBS Tennessee) in violation of ERISA Section 406(a)(1)(A).

ERISA Section 406(a)(1)(D) prohibits a plan fiduciary from causing a plan to engage in a transaction if the fiduciary knows or should know that the transaction constitutes a direct or indirect transfer to, or use by or for the benefit of, a party-in-interest, of the income or assets of the plan. The transfer of Plan assets to BCBS Tennessee in connection with the Repayment would constitute an impermissible transfer of Plan assets to a party-in-interest in violation of ERISA Section 406(a)(1)(D).

#### Conditions

21. This proposed exemption contains a number of conditions that must be met. For example, the proposed exemption mandates that the Independent Fiduciary, in full accordance with its obligations of prudence and loyalty under ERISA Section 404(a)(1)(A) and (B) must:

(a) review, negotiate, and approve the terms and conditions of the Required Restorative Payment, the Repayment, and the Contribution and Assignment Agreement, before the Plan enters into such payments and the agreement;

(b) determine that the terms and conditions of the Required Restorative Payment, the Repayment, and the Contribution and Assignment Agreement are prudent, in the interest of the Plan and its participants and beneficiaries, and protective of the rights of the Plan's participants and beneficiaries;

(c) confirm that the Required Restorative Payment was fully and timely made;

(d) monitor the Claims and confirm that the Plan receives its proper share of any litigation or settlement proceeds received by the Trust in connection with the Claims;

(e) ensure that any Repayment by the Plan to BCBS Tennessee fully complies with the terms of this exemption and is for no more than the lesser of the total Restorative Payment actually made to the Plan by BCBS Tennessee or the amount the Plan received from the Claims, plus Attorney Fees;

(f) ensure that any Repayment by the Plan to BCBS Tennessee for legal expenses in connection with the Claims is limited to only reasonable legal expenses that were paid by BCBS Tennessee to unrelated third parties for representation of the Plan and its interests (as opposed to representation of BCBS Tennessee or the interests of any party other than the Plan) where BCBS Tennessee was not otherwise reimbursed from a non-Plan party;

(g) monitor the Plan's Assigned Interests on an ongoing basis to determine and confirm that any excess recovery amount from the Claims (i.e., any amount that exceeds the Required Restorative Payment Amount) is retained by the Plan;

(h) ensure that all of the conditions and definitions of this proposed exemption are met; and

(i) represent that it has not and will not enter into any agreement or instrument that violates ERISA Section 410 or Department Regulations codified at 29 CFR section 2509.75-4.<sup>83</sup>

22. This proposed exemption also requires Gallagher to respond in writing to any information requests from the Department regarding Gallagher's activities as the Plan's Independent Fiduciary. Additionally, no later than 90 days after the resolution of the litigation, Gallagher must submit a written report to the Department demonstrating that all terms and conditions of the exemption have been met.

23. This proposed exemption requires that the Plan has not and will not release any claims, demands and/or causes of action it may have against: (a) any fiduciary of the Plan; (b) any fiduciary of the Trust; (c) BCBS Tennessee; and/or (d) any person or entity related to a person or entity described in (a)-(c) of this paragraph. Additionally, any Repayment by the Plan to BCBS Tennessee must be made in a manner designed to minimize unnecessary costs and disruption to the Plan and its investments.

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<sup>83</sup> ERISA Section 410 provides, in part, that "except as provided in ERISA Sections 405(b)(1) and 405(d), any provision in an agreement or instrument which purports to relieve a fiduciary from responsibility or liability for any responsibility, obligation, or duty under this part [meaning Part 4 of Title I of ERISA] shall be void as against public policy."

24. The Plan may not make any Repayment to BCBS Tennessee before the date: the Plan has received from BCBS Tennessee the entire amount of the Restorative Payment agreed to in the Amended Contribution and Assignment Agreement; and all the Claims are settled. Furthermore, the Plan may not pay any interest to BCBS Tennessee in connection with its receipt of the Required Restorative Payment, nor pledge Plan assets to secure any portion of the Required Restorative Payment.

25. Pursuant to this proposed exemption, the Plan may not incur any expenses, commissions or transaction costs in connection with the Proposed Transactions. However, as noted above, under certain circumstances the Plan may reimburse BCBS Tennessee for reasonable legal expenses arising from the Claims that BCBS Tennessee paid to non-BCBS Tennessee-related parties for representation of the Plan and its interests (as opposed to representation of BCBS Tennessee or the interests of any party other than the Plan) where BCBS Tennessee was not otherwise reimbursed by a non-Plan party.

26. Finally, the exemptive relief provided under this proposed exemption is conditioned upon the Department's assumption that the material facts and representations set forth above in the Summary of Facts and Representation section are true and accurate at all times. In the event that a material fact or representation detailed above is

untrue or inaccurate, the exemptive relief provided under this exemption will cease immediately.

### Statutory Findings

27. ERISA Section 408(a) provides, in part, that the Department may not grant an exemption unless the Department finds that the exemption is administratively feasible, in the interest of affected plans and of their participants and beneficiaries, and protective of the rights of such participants and beneficiaries. Each of these criteria is discussed below.

a. The Proposed Exemption Is "Administratively Feasible." The Department has tentatively determined that the proposed exemption is administratively feasible because, among other things, the Independent Fiduciary will represent the interests of the Plan for all purposes with respect to the Proposed Transactions.<sup>84</sup> In this regard, not later than 90 days after the resolution of the litigation, the Independent Fiduciary must submit a written report to the Department demonstrating that all of the requirements of this exemption have been met.

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<sup>84</sup> This proposed exemption would require that if the Independent Fiduciary resigns, is removed, or for any reason is unable to serve as an Independent Fiduciary, the successor Independent Fiduciary must, among other things, assume all of the duties of the outgoing Independent Fiduciary. As soon as possible, including before the appointment of a successor Independent Fiduciary, the Plan Sponsor and the Plan must notify the Department's Office of Exemption Determinations of the change in Independent Fiduciaries. The notification must contain all material information including the qualifications of the successor Independent Fiduciary.

b. The Proposed Exemption Is "In the Interests of the Plan." The Department has tentatively determined that the proposed exemption is in the interest of the Plan because, among other things, the Plan's receipt of the Required Restorative Payment substantially improved the Plan's funding status, which enhanced the Plan's ability to meet its obligations to fund benefit obligations to participants and beneficiaries and help the Plan avoid the imposition of benefit limitations imposed under Code section 436.

c. The Proposed Exemption Is "Protective of the Plan." The Department has tentatively determined that the proposed exemption is protective of the rights of the Plan's participants and beneficiaries because, among other things, the Plan will repay BCBS Tennessee the lesser of the Required Restorative Payment Amount received, or the amount the Plan receives in proceeds from the Claims, ensuring that the Proposed Transactions will result in an increase in Plan assets of at least the total amount of Restorative Payment (less reasonable legal expenses related to the Claims paid by BCBS Tennessee to unrelated third parties, as confirmed and approved by the Independent Fiduciary). Further, this exemption preserves any right, claim, demand and/or cause of action the Plan may have against: (a) any fiduciary of the Plan; (b) any fiduciary of the Trust; (c) BCBS Tennessee; and/or (d) any person or entity related to a person or entity described in (a)-(c).



### Summary

28. Based on the conditions described above, the Department has tentatively determined that the relief sought by the Applicant satisfies the statutory requirements under ERISA Section 408(a) for the Department to make findings that support its issuance of a proposed exemption.

### **PROPOSED EXEMPTION**

The Department is considering granting an exemption under the authority of ERISA Section 408(a) and Code Section 4975(c)(2) and in accordance with the procedures set forth in the Department's exemption procedure regulation.<sup>85</sup>

### **Section I. Definitions**

(a) The term "Attorney Fees" means reasonable legal expenses paid by BCBS Tennessee on behalf of the Plan in connection with the Claims, if such fees are reviewed and approved by a qualified independent fiduciary who confirms that the fees were reasonably incurred and paid by BCBS Tennessee to unrelated third parties. For the purposes of this exemption, the Attorney Fees reimbursable to BCBS Tennessee do not include: (1) legal expenses paid by the Plan; and (2) legal expenses paid by BCBS Tennessee for

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<sup>85</sup> 29 CFR part 2570, subpart B (55 FR 32836, 32847, August 10, 1990).

representation of BCBC Tennessee or the interests of any party other than the Plan.

(b) The term "BCBS Tennessee" means BlueCross BlueShield of Tennessee, Inc.

(c) The term "Claims" means the legal claims against Allianz Global Investors U.S. LLC (Allianz) and Aon Investments USA Inc. (Aon), to recover certain losses incurred by the Plan in the first quarter of 2020.

(d) The term "Contribution and Assignment Agreement" means the written agreement between BCBS Tennessee and the Plan, dated October 8, 2020, containing all material terms regarding Tennessee's agreement to make the Required Restorative Payment to the Plan in return for the Plan's potential Repayment to BCBS Tennessee of an amount that is no more than lesser of the Required Restorative Payment Amount (as described in Section I(h)) received or the amount of litigation proceeds the Plan receives from the Claims, plus reasonable attorney fees paid to unrelated third parties by BCBS Tennessee in connection with the Claims.

(e) The term "Independent Fiduciary" means Gallagher Fiduciary Advisors, LLC (Gallagher) or a successor Independent Fiduciary to the extent Gallagher or the successor Independent Fiduciary continues to serve in such capacity who:

(1) Is not an affiliate of BCBS Tennessee and does not hold an ownership interest in BCBS Tennessee or affiliates of BCBS Tennessee;

(2) Was not a fiduciary with respect to the Plan before its appointment to serve as the Independent Fiduciary;

(3) Has acknowledged in writing that it:

(i) is a fiduciary with respect to the Plan and has agreed not to participate in any decision regarding any transaction in which it has an interest that might affect its best judgment as a fiduciary; and

(ii) Has appropriate technical training or experience to perform the services contemplated by the exemption;

(4) Has not entered into any agreement or instrument that violates the prohibitions on exculpatory provisions in ERISA Section 410 or the Department's regulation relating to indemnification of fiduciaries;<sup>86</sup>

(5) Has not received gross income from BCBS Tennessee or its affiliates during any fiscal year in an amount that exceeds two percent (2%) of the Independent Fiduciary's gross income from all sources for the prior fiscal year. This provision also applies to a partnership or corporation of which the Independent Fiduciary is an officer, director, or 10 percent (10%) or more partner or

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<sup>86</sup> 29 CFR 2509.75-4.

shareholder, and includes as gross income amounts received as compensation for services provided as an independent fiduciary under any prohibited transaction exemption granted by the Department; and

(6) No organization or individual that is an Independent Fiduciary, and no partnership or corporation of which such organization or individual is an officer, director, or ten percent (10%) or more partner or shareholder, may acquire any property from, sell any property to, or borrow any funds from BCBS Tennessee or from affiliates of BCBS Tennessee while serving as an Independent Fiduciary. This prohibition will continue for six months after the party ceases to be an Independent Fiduciary and/or the Independent Fiduciary negotiates any transaction on behalf of the Plan during the period that the organization or individual serves as an Independent Fiduciary.

(f) The "Plan" means the BlueCross BlueShield of Tennessee, Inc. Pension Plan.

(g) The term "Plan Losses" means the \$93,576,015 in Plan losses the BCBSA's National Employee Benefits Committee alleges were the result of breaches of fiduciary responsibilities and breaches of contract by Allianz Global Investors U.S. LLC and/or Aon Investments USA Inc.

(h) The term "Restorative Payment" means the payment made by BCBS Tennessee to the Plan in connection with the

Plan Losses, defined above, consisting of a \$100,000,000 payment that BCBS Tennessee contributed to the Plan on October 8, 2020. This \$100,000,000 payment is the Required Restorative Payment Amount.

(i) The "Repayment" means the payment, if any, that the Plan will transfer to BCBS Tennessee following the Plan's receipt of proceeds from the Claims, where the Repayment is made following the full and complete resolution of the Claims; and in a manner that is consistent with the terms of the exemption.

## **Section II. Proposed Transactions**

If the proposed exemption is granted, the restrictions of ERISA Sections 406(a)(1)(A), (B) and (D) and the sanctions resulting from the application of Code Section 4975, by reason of Code Sections 4975(c)(1)(A), (B) and (D), shall not apply, effective September 15, 2020, to the following transactions: BCBS Tennessee's transfer of the Restorative Payment to the Plan; and, in return, the Plan's Repayment of an amount to BCBS Tennessee, which must be no more than the lesser of the Restorative Payment Amount received or the amount of litigation proceeds the Plan received from the Claims, plus reasonable Attorney Fees, provided that the Definitions set forth in Section I and the Conditions set forth in Section III are met.

### **Section III. Conditions**

(a) The Plan received the entire Restorative Payment Amount no later than October 8, 2020;

(b) In connection with its receipt of the Required Restorative Payment, the Plan does not release any claims, demands and/or causes of action the Plan may have against the following: (1) any fiduciary of the Plan; (2) any fiduciary of the Trust; (3) BCBS Tennessee; and/or (4) any person or entity related to a person or entity identified in (1)-(3) of this paragraph;

(c) The Plan's Repayment to BCBS Tennessee is for no more than the lesser of the total Restorative Payment received by the Plan or the amount of litigation proceeds the Plan receives from the Claims. The Plan's Repayment to BCBS Tennessee may only occur after the Independent Fiduciary has determined that: all the conditions of the exemption are met; the Plan has received the entirety of the Restorative Payment it is due; and the Plan has received all the litigation proceeds it is due. The Plan's Repayment to BCBS Tennessee must be carried out in a manner designed to minimize unnecessary costs and disruption to the Plan and its investments;

(d) A qualified independent fiduciary (the Independent Fiduciary, as further defined in Section II(e)), acting solely on behalf of the Plan in full accordance with its

obligations of prudence and loyalty under ERISA Sections 404(a)(1)(A) and (B) must:

(1) Review, negotiate and approve the terms and conditions of the Restorative Payment and the Repayment and the Contribution and Assignment Agreement, all of which must be in writing, before the Plan enters into those transactions/agreement;

(2) Determine that the Restorative Payment, the Repayment, and the terms of the Contribution and Assignment Agreement, are prudent and in the interest of the Plan and its participants and beneficiaries;

(3) Confirm that the Required Restorative Payment Amount was fully and timely made;

(4) Monitor the litigation related to the Claims and confirm that the Plan receives, in a timely manner, its proper share of any litigation or settlement proceeds received by the Trust;

(5) Ensure that any Repayment by the Plan to BCBS Tennessee for legal expenses in connection with the Claims is limited to only reasonable legal expenses that were paid by BCBS Tennessee to unrelated third parties;

(6) Ensure that all of the conditions and definitions of this proposed exemption are met;

(7) Submit a written report to the Department's Office of Exemption Determinations demonstrating and

confirming that the terms and conditions of the exemption were met, within 90 days after the Repayment; and

(8) Not enter into any agreement or instrument that violates ERISA Section 410 or the Department's Regulations codified at 29 CFR Section 2509.75-4.

(f) The Plan pays no interest in connection with the Restorative Payment;

(g) The Plan does not pledge any Plan assets to secure any portion of the Restorative Payment;

(h) The Plan does not incur any expenses, commissions, or transaction costs in connection with the Proposed Transactions. However, if first approved by the Independent Fiduciary, the Plan may reimburse BCBS Tennessee for reasonable legal expenses paid in connection with the Claims by BCBS Tennessee to non-BCBS Tennessee-related parties. For purposes of determining the amount of Attorney Fees the Plan may reimburse to BCBS Tennessee under this proposal, the amount of reasonable attorney fees paid by BCBS Tennessee on behalf of the Plan in connection with the Claims must be reduced by the amount of legal fees received by BCBS Tennessee in connection with the Claims from any non-Plan party (i.e., pursuant to a court award);

(i) The proposed transactions do not involve any risk of loss to either the Plan or the Plan's participants and beneficiaries;



(j) No party associated with this exemption has or will indemnify the Independent Fiduciary and the Independent Fiduciary will not request indemnification from any party, in whole or in part, for negligence and/or any violation of state or federal law that may be attributable to the Independent Fiduciary in performing its duties to the Plan with respect to the Proposed Transactions. In addition, no contract or instrument may purport to waive any liability under state or federal law for any such violation.

(k) If an Independent Fiduciary resigns, is removed, or for any reason is unable to serve as an Independent Fiduciary, the Independent Fiduciary must be replaced by a successor entity that: (1) meets the definition of Independent Fiduciary detailed above in Section II(e); and (2) otherwise meets all of the qualification, independence, prudence and diligence requirements set forth in this exemption. Further, any such successor Independent Fiduciary must assume all of the duties of the outgoing Independent Fiduciary. As soon as possible, including before the appointment of a successor Independent Fiduciary, BCBS Tennessee must notify the Department's Office of Exemption Determinations of the change in Independent Fiduciary and such notification must contain all material information regarding the successor

Independent Fiduciary, including the successor Independent Fiduciary's qualifications; and

(1) All of the material facts and representations set forth in the Summary of Facts and Representation are true and accurate at all times.

#### NOTICE TO INTERESTED PERSONS

The Applicant will give notice of the proposed exemption to all interested persons and all of the parties to the litigation described above, within fifteen calendar days after the publication of the notice of proposed exemption in the *Federal Register*. The notice will contain a copy of the notice of proposed exemption, as published in the *Federal Register*, and a supplemental statement, as required pursuant to the Department's regulations codified at 29 CFR 2570.43(a)(2). The supplemental statement will inform interested persons of their right to comment on the pending exemption. Written comments are due by [INSERT DATE THAT IS 45 DAYS FROM THE PUBLICATION OF THE NOTICE IN THE *FEDERAL REGISTER*].

All comments will be made available to the public.

**Warning:** If you submit a comment, EBSA recommends that you include your name and other contact information in the body of your comment, but DO NOT submit information that you consider to be confidential, or otherwise protected (such as a Social Security number or an unlisted phone number) or

confidential business information that you do not want publicly disclosed. All comments may be posted on the Internet and can be retrieved by most Internet search engines.

*For Further Information Contact:* Ms. Blessed Chuksorji-Keefe of the Department, telephone (202) 693-8567. (This is not a toll-free number.)

**Triple-S Management Corporation**

**Located in San Juan, Puerto Rico**

**[Application No. D-12042]**

### **Proposed Exemption**

The Department is considering granting an exemption under the authority of Section 408(a) of the Employee Retirement Income Security Act of 1974, as amended (ERISA), and Section 4975(c)(2) of the Internal Revenue Code of 1986, as amended (the Code). The proposed exemption relates to legal actions and claims (the Claims) against Allianz Global Investors U.S. LLC (Allianz) and Aon Investments USA Inc. (Aon), that arose from certain losses incurred by the Triple-S Management Corporation Non-Contributory Retirement Plan (the Plan) in the first quarter of 2020.<sup>87</sup>

This proposed exemption would permit the past payment of \$10,000,000 by Triple-S Management Corporation (Triple-S), the Plan sponsor, to the Plan (the Restorative

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<sup>87</sup> In proposing this exemption, the Department is not expressing an opinion regarding the merits of any Claim against Allianz and Aon, or whether the Plan's fiduciaries met their fiduciary duties with respect to Plan assets that are the subject of the Claims. Further, in proposing this exemption, the Department is not limiting any party's claim, demand and/or cause of action arising from the Plan's 2020 first quarter losses in any way. Among other things, this exemption preserves any right, claim, demand and/or cause of action the Plan may have against the following: (1) any fiduciary of the Plan; (2) any fiduciary of the Trust; (3) Triple-S Management Corporation and/or (4) any person or entity related to a person or entity described in (1)-(3).

Payment). If the Plan receives litigation proceeds from the Claims, the Plan will transfer the lesser of the litigation proceeds amount or the Restorative Payment amount, plus reasonable attorney fees to Triple-S.

#### **SUMMARY OF FACTS AND REPRESENTATIONS<sup>88</sup>**

1. Triple-S is an insurance holding company that provides health insurance products and services. Triple-S is the only independent licensee of the Blue Cross Blue Shield Association (BCBSA) in Puerto Rico and has a presence in markets such as the U.S. Virgin Islands and Costa Rica.

2. The Plan is an ERISA-covered qualified defined benefit pension plan that covers eligible employees or participants of Triple-S. The Plan was amended effective January 31, 2017, to freeze benefit accruals as of that date with respect to all participants. As of August 31, 2020, the Plan covered 1,144 participants and held \$64,771,505 in total assets.

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<sup>88</sup> The Department notes that availability of this exemption is subject to the express condition that the material facts and representations contained in application D-12042 are true and complete at all times and accurately describe all material terms of the transactions covered by the exemption. If there is any material change in a transaction covered by the exemption or in a material fact or representation described in the application, the exemption will cease to apply as of the date of such change. The Summary of Facts and Representations is based on the Applicant's representations, as well as factual representations contained in the Claims' cause of action (as described below) and does not reflect factual findings or opinions of the Department, unless indicated otherwise.

3. The Plan holds a beneficial interest in the Blue Cross and Blue Shield National Retirement Trust (the Trust). The Trust is a master trust that holds the assets of 16 defined benefit pension plans that participate in the BCBSA's National Retirement Program (the Participating Plans). Northern Trust serves as Trustee and asset custodian to the Trust and maintains separate records that reflect the net asset value of each Participating Plan. The Trust's earnings, market adjustments, and administrative expenses are allocated among the Participating Plans based on the respective Participating Plan's share of the Trust's assets. A Participating Plan's interest in the Trust's net assets is based on its share of the Trust.

4. The Committee serves as named fiduciary and administrator for each Participating Plan. The Committee is a standing committee of the BCBSA's board of directors. In 2011, the Committee invested a portion of the Trust's assets in funds managed by Allianz Global Investors U.S. LLC (Allianz), as part of a Structured Alpha Investment Strategy. These funds included: (a) AllianzGI Structured Alpha Multi-Beta Series LLC I; (b) AllianzGI Structured Alpha Emerging Markets Equity 350 LLC; and (c) AllianzGI Structured Alpha 1000 LLC (collectively, the Structured Alpha Funds).

5. The Applicant represents that the Allianz Structured Alpha strategy consisted of alpha and beta components. According to the applicant, the alpha component was an options trading strategy that Allianz claimed would seek targeted positive return potential while maintaining structural risk protections. The beta component was intended to provide broad market exposure to a particular asset class through investments in financial products similar to an exchange-traded fund that replicates the performance of a market index, such as the S&P 500. According to the Applicant, Allianz represented that the Structured Alpha Strategy would capitalize on the return-generating features of option selling (short volatility) while simultaneously benefitting from the risk-control attributes associated with option buying (long volatility). According to the Applicant, Allianz represented further that the alpha component would include position hedging consisting of long-volatility positions designed to protect the portfolio in the event of a market crash.

6. As of December 31, 2019, the total market value of the Plan's portion of the Trust's investment in the Allianz Structured Alpha Funds was \$127,024,812, which represented 77.66% of total Plan assets.<sup>89</sup>

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<sup>89</sup> By proposing this exemption, the Department does not, in any way, suggest a conclusion that the Plan's fiduciaries met their ERISA Section 404 duties when they caused the Trust to invest 77.66% of the Plan's total assets in the Allianz Structured Alpha Funds.

7. In 2009, the Committee retained Aon (then called Ennis Knupp) to provide investment advice regarding the investment of Plan assets held in the Trust. The Applicant represents that Aon provided regular investment advice pursuant to a written contract between it and the Committee. Pursuant to its engagement, Aon agreed to provide the following: "recommendations to [the Committee] regarding asset allocation" within the Trust; "recommendations to [the Committee] regarding the specific asset allocation and other investment guidelines" for the Trust's investment managers such as Allianz; and advice "regarding the diversification of assets" held in the Trust." The Applicant represents that Aon agreed to: conduct "active, ongoing monitoring" of Allianz to "identify any forward-looking" risks "that could impact performance;" and "inform itself" of any information necessary to discharge its duty to monitor, including information about the actual options positions Allianz had constructed.

8. The Applicant represents that when equity markets sharply declined in February and March of 2020, volatility spiked and the options positions held within the Structured Alpha Strategy were exposed to a heightened risk of loss. The Applicant represents that, unbeknownst to the Committee, and in violation of Allianz's stated investment strategy, Allianz abandoned the hedging strategy that was



the supposed cornerstone of the Structured Alpha Strategy, leaving the portfolio almost entirely unhedged against a spike in market volatility. As described in the Claims, although Allianz had represented that it would buy hedges at strike prices ranging from 10% to 25% below the market, the hedges it actually held at the end of February 2020 were as much as 60% below the market.

The Applicant represents that, as of January 31, 2020, the Trust had invested approximately \$2,916,049,486 in the Structured Alpha Strategy. Six weeks later, the Trust faced a margin call, which the Applicant states left it no choice but to liquidate the investment. The Trust was ultimately able to redeem only \$646,762,678 of its \$2,916,049,486 investment, resulting in a total loss of \$2,269,286,808.

Specifically, regarding the Plan's portion of the loss, as of December 31, 2019 the market value of Plan assets was \$163,558,110. As of March 31, 2020, the market value of Plan assets decreased to \$54,855,395. The Applicant represents that the Plan's total losses from the Allianz Structured Alpha Strategy were \$103,793,253, which caused the Plan to be underfunded.

9. On September 16, 2020, the Committee filed a cause of action in the United States District Court for the Southern District of New York (Case number 20-CIV-07606) against Allianz and Aon for Breach of Fiduciary Duty under

ERISA Section 404, Breach of Co-Fiduciary Duty under ERISA Section 405, and violation of ERISA Section 406(b) for managing the Plan assets in its self-interest and breach of contract. It is possible that resolution of this claim and other legal actions against Allianz and Aon in connection with the Plan's losses (the Claims) could take an extended period of time.

10. The Applicant states that rather than wait for the Claims to be resolved, Triple-S took steps to protect Plan benefits and avoid onerous benefit restrictions under Code section 436 that could apply to the Plan as a result of a funding shortfall. Therefore, on November 6, 2020, Triple-S and the Plan entered into a Contribution and Assignment Agreement whereby Triple-S agreed to make a \$10,000,000 Restorative Payment to the Plan not later than December 31, 2021 (the Contribution and Assignment Agreement). Subsequently, on June 28, 2021, Triple-S made a \$10,000,000 Restorative Payment to the Plan.

11. In exchange for the Restorative Payment, the Plan assigned to Triple-S its right to retain certain litigation and/or settlement proceeds recovered from the Claims (the Assigned Interests).<sup>90</sup> Per the assignment, once the Allianz/Aon litigation is resolved and if the Plan receives

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<sup>90</sup> Under the Contribution and Assignment Agreement, if the Plan receives litigation or settlement proceeds from the Claims, the proceeds would first flow to the Trust, and then each Plan's pro rata portion of the proceeds would be deposited into the individual trust funding that Plan.

litigation proceeds from the Claims, the Plan will transfer to Triple-S a repayment (the Repayment) that does not exceed the total Restorative Payment made by Triple-S as of that date, plus reasonable attorney fees paid by Triple-S on behalf of the Plan in connection with the Claims, if such fees are reviewed and approved by a qualified independent fiduciary who confirms that the fees were reasonably incurred and paid by Triple-S to unrelated third parties (the Attorney Fees).

For the purposes of this exemption, Attorney Fees reimbursable to Triple-S do not include: (a) legal expenses paid by the Plan; and (b) legal expenses paid by Triple-S for representation of its own interests or the interests of any party other than the Plan. For purposes of determining the amount of Attorney Fees the Plan may reimburse to Triple-S under this exemption, the amount of reasonable attorney fees paid by Triple-S on behalf of the Plan in connection with the Claims must be reduced by the amount of legal fees received by Triple-S in connection with the Claims from any non-Plan party (for example, from a third party pursuant to a court award).

12. The Plan must ultimately receive at least the full value of the promised Restorative Payment, minus the Attorney Fees. The Plan may ultimately receive more than the Restorative Payment amount required under the Contribution and Assignment Agreement. If the Plan

receives litigation or settlement proceeds that exceed the amount of Restorative Payment that Triple-S has made to the Plan, the Plan's Repayment to Triple-S will be limited to the Restorative Payment amount, plus Attorney Fees. For example, if Triple-S reasonably incurred \$100,000 in Attorney Fees, and the Plan receives \$20,000,000 in litigation proceeds, the Plan will make a Repayment to Triple-S totaling \$10,100,000.

13. Alternatively, if the Plan receives less litigation or settlement proceeds than the amount of the Restorative Payment, the Plan will transfer to Triple-S the lesser amount of litigation or settlement proceeds, plus Attorney Fees. For example, if Triple-S reasonably incurred \$100,000 in Attorney Fees, and the Plan receives \$5,000,000 in litigation proceeds, the Plan will make a Repayment to Triple-S totaling \$5,100,000.

14. The Department notes that if the Plan receives any restitution that is tied to the conduct underlying the Claims but was ordered pursuant to a proceeding or directive that is external to Case number 20-CIV-07606, the disposition of such proceeds must conform to the requirements of this exemption.

15. Triple-S retained Gallagher Fiduciary Advisors, LLC (Gallagher or the Independent Fiduciary) of New York, New York, to serve as the Plan's independent fiduciary with respect to the Required Restorative Payment and the

potential repayment by the Plan of those Payments (collectively, the Proposed Transactions). Gallagher represents that it has extensive experience in institutional investment consulting and fiduciary decision-making regarding traditional and alternative investments. Gallagher further represents that its independent fiduciary decision-making work involves acting as a fiduciary advisor or decision-maker for plans and other ERISA-regulated asset pools and that it has experience with a wide range of asset classes and litigation claims.

16. Gallagher represents that it understands its duties and responsibilities under ERISA in acting as a fiduciary on behalf of the Plan. Gallagher also acknowledges that it is authorized to take all appropriate actions to safeguard the Plan's interests, and that it will monitor the Proposed Transactions on the Plan's behalf on a continuous basis and throughout the term required by this exemption.

17. Gallagher represents that it does not have any prior relationship with any parties in interest to the Plan, including Triple-S and any Triple-S affiliates. Gallagher further represents the total revenues it has received from the Plan and from parties in interest to the Plan in connection with its engagement as Independent Fiduciary represents approximately 0.78% of Gallagher's total revenue.

18. Gallagher represents that no party associated with this exemption application has or will indemnify it, in whole or in part, for negligence of any kind and/or any violation of state or federal law that may be attributable to Gallagher's performance of its duties as Independent Fiduciary to the Plan with respect to the Proposed Transactions. In addition, no contract or instrument entered into by Gallagher as Independent Fiduciary may purport to waive any liability under state or federal law for any such violation.

19. On November 5, 2020, Gallagher completed an Independent Fiduciary Report (the Independent Fiduciary Report) finding that the massive losses caused by the Trust's investment in the Allianz Structured Alpha Strategy resulted in a significant reduction to the Plan's total assets and funding level. Gallagher represents that the Required Restorative Payment, which will be received by the Plan substantially in advance of a final resolution of the Claims against Allianz and Aon, should restore the Plan's funded percentage to its pre-loss funded percentage as of January 1, 2019. The restoration of the Plan's funding status will secure ongoing benefit payments to participants and beneficiaries.

Gallagher notes that the Contribution and Assignment Agreement provides that the Trust must reimburse Triple-S only up to the Required Restorative Payment Amount received

by the Plan, plus any reasonable legal expense paid to non-Triple-S-related parties that were incurred by, or allocated to, Triple-S as a result of the Claims.<sup>91</sup> Thus, if the Plan's ultimate recovery amount from the Claims is less than the Required Restorative Payment Amount, plus related litigation expenses that were allocated to the Plan, Triple-S, not the Plan, will suffer the loss.

Gallagher states that the Proposed Transactions and the terms of the Contribution and Assignment Agreement were negotiated and approved by Gallagher in its role as the Plan's Independent Fiduciary. Gallagher states that it approved the Proposed Transactions only after conducting an extensive analysis of the damages suffered by the Plan as a result of the failed Allianz Structured Alpha Strategy. Gallagher represents that it conducted numerous discussions with Trust representatives and counsel, along with the Plan's representatives and counsel to ensure that the interests of the Plan's participants and beneficiaries were protected with respect to all aspects of the Proposed Transactions. Based upon its assessment, Gallagher approved the Plan's receipt of the Required Restorative Payment from Triple-S in exchange for the Assignment.

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<sup>91</sup> Currently, legal fees and expenses associated with the Claims are being paid by most of the Participating Plan's trusts on a pro rata basis according to each Participating Plan's total invested assets held in the Master Trust's Allianz Structured Alpha Strategy before the losses were incurred in the first quarter 2020. The Applicant represents that the Committee reviews and approves these legal fees before passing them through to each Participating Plan.

## ERISA Analysis

20. Absent an exemption, the Plan's receipt of the Restorative Payment from Triple-S in exchange for the Plan's transfer of litigation or settlement proceeds to Triple-S would violate ERISA. In this regard, ERISA Section 406(a)(1)(A) prohibits a plan fiduciary from causing the plan to engage in a transaction if the fiduciary knows or should know that such transaction constitutes a direct or indirect sale or exchange of any property between a plan and a party in interest. Triple-S, as an employer whose employees are covered by the Plan, is a party in interest with respect to the Plan under ERISA Section 3(14)(C). The Required Restorative Payment to the Plan and the Plan's potential repayment to Triple-S with litigation or settlement proceeds would constitute impermissible exchanges between the Plan and a party-in-interest (Triple-S) in violation of ERISA Section 406(a)(1)(A).

ERISA Section 406(a)(1)(B) prohibits the lending of money or other extension of credit between a plan and a party-in-interest. Triple's promise to make the Required Restorative Payment to the Plan, over time, constitutes an impermissible extension of credit between the Plan and a party-in-interest in violation of ERISA Section 406(a)(1)(B).



ERISA Section 406(a)(1)(D) prohibits a plan fiduciary from causing a plan to engage in a transaction if the fiduciary knows or should know that the transaction constitutes a direct or indirect transfer to, or use by or for the benefit of, a party-in-interest, of the income or assets of the plan. The transfer of Plan assets to Triple-S in connection with the Repayment would constitute an impermissible transfer of Plan assets to a party-in-interest in violation of ERISA Section 406(a)(1)(D).

#### Conditions

21. This proposed exemption contains a number of conditions that must be met. For example, the proposed exemption mandates that the Independent Fiduciary, in full accordance with its obligations of prudence and loyalty under ERISA Section 404(a)(1)(A) and (B) must:

(a) review, negotiate, and approve the terms and conditions of the Required Restorative Payment, the Repayment, and the Contribution and Assignment Agreement, before the Plan enters into such payments and the agreement;

(b) determine that the terms and conditions of the Required Restorative Payment, the Repayment, and the Contribution and Assignment Agreement are prudent, in the interest of the Plan and its participants and beneficiaries, and protective of the rights of the Plan's participants and beneficiaries;

(c) confirm that the Required Restorative Payment was fully and timely made;

(d) monitor the Claims and confirm that the Plan receives its proper share of any litigation or settlement proceeds received by the Trust in connection with the Claims;

(e) ensure that any Repayment by the Plan to Triple-S fully complies with the terms of this exemption and is for no more than the lesser of the total Restorative Payment or the amount the Plan received from the Claims, plus Attorney Fees;

(f) ensure that any Repayment by the Plan to Triple-S for legal expenses in connection with the Claims is limited to only reasonable legal expenses that were paid by Triple-S to unrelated third parties for representation of the Plan and its interests (as opposed to representation of Triple-S or the interests of any party other than the Plan) where Triple-S was not otherwise reimbursed from a non-Plan party;

(g) monitor the Plan's Assigned Interests on an ongoing basis to determine and confirm that any excess recovery amount from the Claims (i.e., any amount that exceeds the Required Restorative Payment Amount) is retained by the Plan;

(h) ensure that all of the conditions and definitions of this proposed exemption are met; and

(i) represent that it has not and will not enter into any agreement or instrument that violates ERISA Section 410 or Department Regulations codified at 29 CFR section 2509.75-4.<sup>92</sup>

22. This proposed exemption also requires Gallagher to respond in writing to any information requests from the Department regarding Gallagher's activities as the Plan's Independent Fiduciary. Additionally, no later than 90 days after the resolution of the litigation, Gallagher must submit a written report to the Department demonstrating that all terms and conditions of the exemption have been met.

23. This proposed exemption requires that the Plan has not and will not release any claims, demands and/or causes of action it may have against: (a) any fiduciary of the Plan; (b) any fiduciary of the Trust; (c) Triple-S; and/or (d) any person or entity related to a person or entity described in (a)-(c) of this paragraph. Additionally, any Repayment by the Plan to Triple-S must be made in a manner designed to minimize unnecessary costs and disruption to the Plan and its investments.

24. The Plan may not make any Repayment to Triple-S before the date: the Plan has received from Triple-S the

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<sup>92</sup> ERISA Section 410 provides, in part, that "except as provided in ERISA Sections 405(b)(1) and 405(d), any provision in an agreement or instrument which purports to relieve a fiduciary from responsibility or liability for any responsibility, obligation, or duty under this part [meaning Part 4 of Title I of ERISA] shall be void as against public policy."

entire amount of the Restorative Payment agreed to in the Amended Contribution and Assignment Agreement; and all the Claims are settled. Furthermore, the Plan may not pay any interest to Triple-S in connection with its receipt of the Required Restorative Payment, nor pledge Plan assets to secure any portion of the Required Restorative Payment.

25. Pursuant to this proposed exemption, the Plan may not incur any expenses, commissions or transaction costs in connection with the Proposed Transactions. However, as noted above, under certain circumstances the Plan may reimburse Triple-S for reasonable legal expenses arising from the Claims that Triple-S paid to non-Triple-S-related parties for representation of the Plan and its interests (as opposed to representation of Triple-S or the interests of any party other than the Plan) where Triple-S was not otherwise reimbursed by a non-Plan party.

26. Finally, the exemptive relief provided under this proposed exemption is conditioned upon the Department's assumption that the material facts and representations set forth above in the Summary of Facts and Representation section are true and accurate at all times. In the event that a material fact or representation detailed above is untrue or inaccurate, the exemptive relief provided under this exemption will cease immediately.

#### Statutory Findings

27. ERISA Section 408(a) provides, in part, that the Department may not grant an exemption unless the Department finds that the exemption is administratively feasible, in the interest of affected plans and of their participants and beneficiaries, and protective of the rights of such participants and beneficiaries. Each of these criteria is discussed below.

a. The Proposed Exemption Is "Administratively Feasible." The Department has tentatively determined that the proposed exemption is administratively feasible because, among other things, the Independent Fiduciary will represent the interests of the Plan for all purposes with respect to the Proposed Transactions.<sup>93</sup> In this regard, not later than 90 days after the resolution of the litigation, the Independent Fiduciary must submit a written report to the Department demonstrating that all of the requirements of this exemption have been met.

b. The Proposed Exemption Is "In the Interests of the Plan." The Department has tentatively determined that the proposed exemption is in the interest of the Plan because, among other things, the Plan's receipt of the Required

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<sup>93</sup> This proposed exemption would require that if the Independent Fiduciary resigns, is removed, or for any reason is unable to serve as an Independent Fiduciary, the successor Independent Fiduciary must, among other things, assume all of the duties of the outgoing Independent Fiduciary. As soon as possible, including before the appointment of a successor Independent Fiduciary, the Plan Sponsor and the Plan must notify the Department's Office of Exemption Determinations of the change in Independent Fiduciaries. The notification must contain all material information including the qualifications of the successor Independent Fiduciary.

Restorative Payment substantially improved the Plan's funding status, which enhanced the Plan's ability to meet its obligations to fund benefit obligations to participants and beneficiaries and help the Plan avoid the imposition of benefit limitations imposed under Code section 436.

c. The Proposed Exemption Is "Protective of the Plan."

The Department has tentatively determined that the proposed exemption is protective of the rights of the Plan's participants and beneficiaries because, among other things, the Plan will repay Triple-S the lesser of the Required Restorative Payment Amount received by the Plan, or the amount the Plan receives in proceeds from the Claims, ensuring that the Proposed Transactions will result in an increase in Plan assets of at least the total amount of Restorative Payment (less reasonable legal expenses related to the Claims paid by Triple-S to unrelated third parties, as confirmed and approved by the Independent Fiduciary). Further, this exemption preserves any right, claim, demand and/or cause of action the Plan may have against: (a) any fiduciary of the Plan; (b) any fiduciary of the Trust; (c) Triple-S; and/or (d) any person or entity related to a person or entity described in (a)-(c).

Summary

28. Based on the conditions described above, the Department has tentatively determined that the relief

sought by the Applicant satisfies the statutory requirements under ERISA Section 408(a) for the Department to make findings that support its issuance of a proposed exemption.

#### **PROPOSED EXEMPTION**

The Department is considering granting an exemption under the authority of ERISA Section 408(a) and Code Section 4975(c)(2) and in accordance with the procedures set forth in the Department's exemption procedure regulation.<sup>94</sup>

#### **Section I. Definitions**

(a) The term "Attorney Fees" means reasonable legal expenses paid by Triple-S on behalf of the Plan in connection with the Claims, if such fees are reviewed and approved by a qualified independent fiduciary who confirms that the fees were reasonably incurred and paid by Triple-S to unrelated third parties. For the purposes of this exemption, the Attorney Fees reimbursable to Triple-S do not include: (1) legal expenses paid by the Plan; and (2) legal expenses paid by Triple-S for representation of Triple-S or the interests of any party other than the Plan.

(b) The term "Triple-S" means Triple-S Management Corporation.

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<sup>94</sup> 29 CFR part 2570, subpart B (55 FR 32836, 32847, August 10, 1990).

(c) The term "Claims" means the legal claims against Allianz Global Investors U.S. LLC (Allianz) and Aon Investments USA Inc. (Aon), to recover certain losses incurred by the Plan in the first quarter of 2020.

(d) The term "Contribution and Assignment Agreement" means the written agreement between Triple-S and the Plan, dated November 6, 2020, containing all material terms regarding Triple-S's agreement to make Required Restorative Payment to the Plan in return for the Plan's potential Repayment to Triple-S of an amount that is no more than lesser of the Required Restorative Payment Amount (as described in Section I(h)) received by the Plan or the amount of litigation proceeds the Plan receives from the Claims, plus reasonable attorney fees paid to unrelated third parties by Triple-S in connection with the Claims.

(e) The term "Independent Fiduciary" means Gallagher Fiduciary Advisors, LLC (Gallagher) or a successor Independent Fiduciary to the extent Gallagher or the successor Independent Fiduciary continues to serve in such capacity who:

(1) Is not an affiliate of Triple-S and does not hold an ownership interest in Triple-S or affiliates of Triple-S;

(2) Was not a fiduciary with respect to the Plan before its appointment to serve as the Independent Fiduciary;



(3) Has acknowledged in writing that it:

(i) is a fiduciary with respect to the Plan and has agreed not to participate in any decision regarding any transaction in which it has an interest that might affect its best judgment as a fiduciary; and

(ii) Has appropriate technical training or experience to perform the services contemplated by the exemption;

(4) Has not entered into any agreement or instrument that violates the prohibitions on exculpatory provisions in ERISA Section 410 or the Department's regulation relating to indemnification of fiduciaries;<sup>95</sup>

(5) Has not received gross income from Triple-S or its affiliates during any fiscal year in an amount that exceeds two percent (2%) of the Independent Fiduciary's gross income from all sources for the prior fiscal year. This provision also applies to a partnership or corporation of which the Independent Fiduciary is an officer, director, or 10 percent (10%) or more partner or shareholder, and includes as gross income amounts received as compensation for services provided as an independent fiduciary under any prohibited transaction exemption granted by the Department; and

(6) No organization or individual that is an Independent Fiduciary, and no partnership or corporation of

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<sup>95</sup> 29 CFR 2509.75-4.

which such organization or individual is an officer, director, or ten percent (10%) or more partner or shareholder, may acquire any property from, sell any property to, or borrow any funds from Triple-S or from affiliates of Triple-S while serving as an Independent Fiduciary. This prohibition will continue for six months after the party ceases to be an Independent Fiduciary and/or the Independent Fiduciary negotiates any transaction on behalf of the Plan during the period that the organization or individual serves as an Independent Fiduciary.

(f) The "Plan" means the Triple-S Management Corporation Non-Contributory Retirement Plan.

(g) The term "Plan Losses" means the \$103,793,253 in Plan losses the BCBSA's National Employee Benefits Committee alleges were the result of breaches of fiduciary responsibilities and breaches of contract by Allianz Global Investors U.S. LLC and/or Aon Investments USA Inc.

(h) The term "Restorative Payment" means the payment made by Triple-S of \$10,000,000 to the Plan in connection with the Plan Losses, defined above, consisting of a \$10,000,000 payment that Triple-S contributed to the Plan on June 28, 2021.

(i) The "Repayment" means the payment, if any, that the Plan will transfer to Triple-S following the Plan's receipt of proceeds from the Claims, where the Repayment is

made following the full and complete resolution of the Claims, and in a manner that is consistent with the terms of the exemption.

## **Section II. Proposed Transactions**

If the proposed exemption is granted, the restrictions of ERISA Sections 406(a)(1)(A), (B), and (D) and the sanctions resulting from the application of Code Section 4975, by reason of Code Sections 4975(c)(1)(A), (B) and (D), shall not apply, effective November 5, 2020, to the following transactions: Triple-S's transfer of Restorative Payment to the Plan; and, in return, the Plan's Repayment of an amount to Triple-S, which must be no more than the lesser of the Restorative Payment received by the Plan or the amount of litigation proceeds the Plan received from the Claims, plus reasonable Attorney Fees, provided that the Definitions set forth in Section I and the Conditions set forth in Section III are met.

## **Section III. Conditions**

(a) The Plan received the entire Restorative Payment Amount no later than June 28, 2021;

(b) In connection with its receipt of the Required Restorative Payment, the Plan does not release any claims, demands and/or causes of action the Plan may have against the following: (1) any fiduciary of the Plan; (2) any

fiduciary of the Trust; (3) Triple-S; and/or (4) any person or entity related to a person or entity identified in (1)-(3) of this paragraph;

(c) The Plan's Repayment to Triple-S is for no more than the lesser of the total Restorative Payment received by the Plan or the amount of litigation proceeds the Plan receives from the Claims. The Plan's Repayment to Triple-S may only occur after the Independent Fiduciary has determined that: all the conditions of the exemption are met; the Plan has received all the Restorative Payments it is due; and the Plan has received all the litigation proceeds it is due. The Plan's Repayment to Triple-S must be carried out in a manner designed to minimize unnecessary costs and disruption to the Plan and its investments;

(d) A qualified independent fiduciary (the Independent Fiduciary, as further defined in Section II(e)), acting solely on behalf of the Plan in full accordance with its obligations of prudence and loyalty under ERISA Sections 404(a)(1)(A) and (B) must:

(1) Review, negotiate and approve the terms and conditions of the Restorative Payment and the Repayment and the Contribution and Assignment Agreement, all of which must be in writing, before the Plan enters into those transactions/agreement;

(2) Determine that the Restorative Payment, the Repayment, and the terms of the Contribution and Assignment

Agreement, are prudent and in the interest of the Plan and its participants and beneficiaries;

(3) Confirm that the Required Restorative Payment Amount was fully and timely made;

(4) Monitor the litigation related to the Claims and confirm that the Plan receives, in a timely manner, its proper share of any litigation or settlement proceeds received by the Trust;

(5) Ensure that any Repayment by the Plan to Triple-S for legal expenses in connection with the Claims is limited to only reasonable legal expenses that were paid by Triple-S to unrelated third parties;

(6) Ensure that all of the conditions and definitions of this proposed exemption are met;

(7) Submit a written report to the Department's Office of Exemption Determinations demonstrating and confirming that the terms and conditions of the exemption were met, within 90 days after the Repayment; and

(8) Not enter into any agreement or instrument that violates ERISA Section 410 or the Department's Regulations codified at 29 CFR Section 2509.75-4.

(f) The Plan pays no interest in connection with the Restorative Payment;

(g) The Plan does not pledge any Plan assets to secure any portion of the Restorative Payment;

(h) The Plan does not incur any expenses, commissions, or transaction costs in connection with the Proposed Transactions. However, if first approved by the Independent Fiduciary, the Plan may reimburse Triple-S for reasonable legal expenses paid in connection with the Claims by Triple-S to non-Triple-S-related parties. For purposes of determining the amount of Attorney Fees the Plan may reimburse to Triple-S under this proposal, the amount of reasonable attorney fees paid by Triple-S on behalf of the Plan in connection with the Claims must be reduced by the amount of legal fees received by Triple-S in connection with the Claims from any non-Plan party (i.e., pursuant to a court award);

(i) The proposed transactions do not involve any risk of loss to either the Plan or the Plan's participants and beneficiaries;

(j) No party associated with this exemption has or will indemnify the Independent Fiduciary and the Independent Fiduciary will not request indemnification from any party, in whole or in part, for negligence and/or any violation of state or federal law that may be attributable to the Independent Fiduciary in performing its duties to the Plan with respect to the Proposed Transactions. In addition, no contract or instrument may purport to waive any liability under state or federal law for any such violation.

(k) If an Independent Fiduciary resigns, is removed, or for any reason is unable to serve as an Independent Fiduciary, the Independent Fiduciary must be replaced by a successor entity that: (1) meets the definition of Independent Fiduciary detailed above in Section II(e); and (2) otherwise meets all of the qualification, independence, prudence and diligence requirements set forth in this exemption. Further, any such successor Independent Fiduciary must assume all of the duties of the outgoing Independent Fiduciary. As soon as possible, including before the appointment of a successor Independent Fiduciary, Triple-S must notify the Department's Office of Exemption Determinations of the change in Independent Fiduciary and such notification must contain all material information regarding the successor Independent Fiduciary, including the successor Independent Fiduciary's qualifications; and

(1) All of the material facts and representations set forth in the Summary of Facts and Representation are true and accurate at all times.

#### NOTICE TO INTERESTED PERSONS

The Applicant will give notice of the proposed exemption to all interested persons and all of the parties to the litigation described above, within fifteen calendar days after the publication of the notice of proposed

exemption in the *Federal Register*. The notice will contain a copy of the notice of proposed exemption, as published in the *Federal Register*, and a supplemental statement, as required pursuant to the Department's regulations codified at 29 CFR 2570.43(a)(2). The supplemental statement will inform interested persons of their right to comment on the pending exemption. Written comments are due by [INSERT DATE THAT IS 45 DAYS FROM THE PUBLICATION OF THE NOTICE IN THE *FEDERAL REGISTER*].

All comments will be made available to the public.

**Warning:** If you submit a comment, EBSA recommends that you include your name and other contact information in the body of your comment, but DO NOT submit information that you consider to be confidential, or otherwise protected (such as a Social Security number or an unlisted phone number) or confidential business information that you do not want publicly disclosed. All comments may be posted on the Internet and can be retrieved by most Internet search engines.

*For Further Information Contact:* Ms. Anna Vaughan of the Department, telephone (202) 693-8565. (This is not a toll-free number.)



**National Account Service Company LLC**

**Located in Atlanta, Georgia**

**[Application No. D-12049]**

### **Proposed Exemption**

The Department is considering granting an exemption under the authority of Section 408(a) of the Employee Retirement Income Security Act of 1974, as amended (ERISA), and Section 4975(c)(2) of the Internal Revenue Code of 1986, as amended (the Code). The proposed exemption relates to legal actions and claims (the Claims) against Allianz Global Investors U.S. LLC (Allianz) and Aon Investments USA Inc. (Aon), that arose from certain losses incurred by the Non-Contributory Retirement Program for Certain Employees of National Account Service Company (the Plan) in the first quarter of 2020.<sup>96</sup>

This proposed exemption would permit the Plan sponsor, the National Account Service Company LLC (NASCO), to make payments totaling \$50 million to the Plan (the Restorative

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<sup>96</sup> In proposing this exemption, the Department is not expressing an opinion regarding the merits of any Claim against Allianz and Aon, or whether the Plan's fiduciaries met their fiduciary duties with respect to Plan assets that are the subject of the Claims. Further, in proposing this exemption, the Department is not limiting any party's claim, demand and/or cause of action arising from the Plan's 2020 first quarter losses in any way. Among other things, this exemption preserves any right, claim, demand and/or cause of action the Plan may have against the following: (1) any fiduciary of the Plan; (2) any fiduciary of the Trust; (3) National Account Service Company LLC; and/or (4) any person or entity related to a person or entity described in (1)-(3).

Payments). If the Plan receives litigation proceeds from the Claims, the Plan will transfer the lesser of the litigation proceeds amount or the Restorative Payments, plus reasonable attorney fees to NASCO.

#### **SUMMARY OF FACTS AND REPRESENTATIONS<sup>97</sup>**

1. NASCO is a healthcare technology company dedicated to co-creating digital health solutions for Blue Cross and Blue Shield companies. NASCO provides information technology products and services and offers payment management, system delivery, business optimization solutions, membership enrollment, and other related services. NASCO is owned by Blue Cross Blue Shield of Michigan Mutual Insurance Company.

2. The Plan is an ERISA-covered qualified defined benefit pension plan that covers eligible employees of NASCO. The Plan was amended effective January 1, 2009 to close participation to new entrants as of December 31, 2008. As of December 31, 2020, the Plan covered 264 participants and held \$47,306,049 in total assets.

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<sup>97</sup> The Department notes that availability of this exemption is subject to the express condition that the material facts and representations contained in application D-12049 are true and complete at all times and accurately describe all material terms of the transactions covered by the exemption. If there is any material change in a transaction covered by the exemption or in a material fact or representation described in the application, the exemption will cease to apply as of the date of such change. The Summary of Facts and Representations is based on the Applicant's representations, as well as factual representations contained in the Claims' cause of action (as described below) and does not reflect factual findings or opinions of the Department, unless indicated otherwise.

3. The Plan holds a beneficial interest in the Blue Cross and Blue Shield National Retirement Trust (the Trust). The Trust is a master trust that holds the assets of 16 defined benefit pension plans that participate in the BCBSA's National Retirement Program (the Participating Plans). Northern Trust serves as Trustee and asset custodian to the Trust and maintains separate records that reflect the net asset value of each Participating Plan. The Trust's earnings, market adjustments, and administrative expenses are allocated among the Participating Plans based on the respective Participating Plan's share of the Trust's assets. A Participating Plan's interest in the Trust's net assets is based on its share of the Trust.

4. The Committee serves as named fiduciary and administrator for each Participating Plan. The Committee is a standing committee of the BCBSA's board of directors. In 2011, the Committee invested a portion of the Trust's assets in funds managed by Allianz Global Investors U.S. LLC (Allianz), as part of a Structured Alpha Investment Strategy. These funds included: (a) AllianzGI Structured Alpha Multi-Beta Series LLC I; (b) AllianzGI Structured Alpha Emerging Markets Equity 350 LLC; and (c) AllianzGI Structured Alpha 1000 LLC (collectively, the Structured Alpha Funds).

5. The Applicant represents that the Allianz Structured Alpha strategy consisted of alpha and beta components. According to the applicant, the alpha component was an options trading strategy that Allianz claimed would seek targeted positive return potential while maintaining structural risk protections. The beta component was intended to provide broad market exposure to a particular asset class through investments in financial products similar to an exchange-traded fund that replicates the performance of a market index, such as the S&P 500. According to the Applicant, Allianz represented that the Structured Alpha Strategy would capitalize on the return-generating features of option selling (short volatility) while simultaneously benefitting from the risk-control attributes associated with option buying (long volatility). According to the Applicant, Allianz represented further that the alpha component would include position hedging consisting of long-volatility positions designed to protect the portfolio in the event of a market crash.

6. As of December 31, 2019, the total market value of the Plan's portion of the Trust's investment in the Allianz Structured Alpha Funds was \$63,571,918, which represented 77.66% of total Plan assets.<sup>98</sup>

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<sup>98</sup> By proposing this exemption, the Department does not, in any way, suggest a conclusion that the Plan's fiduciaries met their ERISA Section 404 duties when they caused the Trust to invest 77.66% of the Plan's total assets in the Allianz Structured Alpha Funds.

7. In 2009, the Committee retained Aon (then called Ennis Knupp) to provide investment advice regarding the investment of Plan assets held in the Trust. The Applicant represents that Aon provided regular investment advice pursuant to a written contract between it and the Committee. Pursuant to its engagement, Aon agreed to provide the following: "recommendations to [the Committee] regarding asset allocation" within the Trust; "recommendations to [the Committee] regarding the specific asset allocation and other investment guidelines" for the Trust's investment managers such as Allianz; and advice "regarding the diversification of assets" held in the Trust." The Applicant represents that Aon agreed to: conduct "active, ongoing monitoring" of Allianz to "identify any forward-looking" risks "that could impact performance;" and "inform itself" of any information necessary to discharge its duty to monitor, including information about the actual options positions Allianz had constructed.

8. The Applicant represents that when equity markets sharply declined in February and March of 2020, volatility spiked and the options positions held within the Structured Alpha Strategy were exposed to a heightened risk of loss. The Applicant represents that, unbeknownst to the Committee, and in violation of Allianz's stated investment strategy, Allianz abandoned the hedging strategy that was

the supposed cornerstone of the Structured Alpha Strategy, leaving the portfolio almost entirely unhedged against a spike in market volatility. As described in the Claims, although Allianz had represented that it would buy hedges at strike prices ranging from 10% to 25% below the market, the hedges it actually held at the end of February 2020 were as much as 60% below the market.

The Applicant represents that, as of January 31, 2020, the Trust had invested approximately \$2,916,049,486 in the Structured Alpha Strategy. Six weeks later, the Trust faced a margin call, which the Applicant states left it no choice but to liquidate the investment. The Trust was ultimately able to redeem only \$646,762,678 of its \$2,916,049,486 investment, resulting in a total loss of \$2,269,286,808.

Specifically, regarding the Plan's portion of the loss, as of December 31, 2019 the market value of Plan assets was \$81,855,683. As of March 31, 2020, the market value of Plan assets decreased to \$28,120,905. The Applicant represents that the Plan's total losses from the Allianz Structured Alpha Strategy were \$51,662,561, which caused the Plan to be underfunded.

9. On September 16, 2020, the Committee filed a cause of action in the United States District Court for the Southern District of New York (Case number 20-CIV-07606) against Allianz and Aon for Breach of Fiduciary Duty under

ERISA Section 404, Breach of Co-Fiduciary Duty under ERISA Section 405, and violation of ERISA Section 406(b) for managing the Plan assets in its self-interest and breach of contract. It is possible that resolution of this claim and other legal actions against Allianz and Aon in connection with the Plan's losses (the Claims) could take an extended period of time.

10. The Applicant states that rather than wait for the Claims to be resolved, NASCO took steps to protect Plan benefits and avoid onerous benefit restrictions under Code section 436 that could apply to the Plan as a result of a funding shortfall. Therefore, on March 1, 2021, NASCO and the Plan entered into a Contribution and Assignment Agreement pursuant to which NASCO agreed to make Restorative Payments to the Plan not in excess of \$50,000,000 over the course of 2021 through 2025 (the Contribution and Assignment Agreement).

11. NASCO has made Restorative Payments to the Plan totaling \$22,800,000, including: (a) a \$2,000,000 payment on August 3, 2020; (b) a \$2,000,000 payment on September 2, 2020; (c) a \$3,625,000 payment on June 21, 2021; (d) a \$3,625,000 payment on July 21, 2021; (e) a \$3,625,000 payment on August 16, 2021; (f) a \$3,625,000 payment on September 13, 2021; and (g) a \$4,300,000 payment on June 21, 2021.

12. In exchange for the Restorative Payments, the Plan assigned to NASCO its right to retain certain litigation and/or settlement proceeds recovered from the Claims (the Assigned Interests).<sup>99</sup> Per the assignment, once the Allianz/Aon litigation is resolved and if the Plan receives litigation proceeds from the Claims, the Plan will transfer to NASCO a repayment (the Repayment) that does not exceed the total Restorative Payments made by NASCO as of that date, plus reasonable attorney fees paid by NASCO on behalf of the Plan in connection with the Claims, if such fees are reviewed and approved by a qualified independent fiduciary who confirms that the fees were reasonably incurred and paid by NASCO to unrelated third parties (the Attorney Fees).

For the purposes of this exemption, Attorney Fees reimbursable to NASCO do not include: (a) legal expenses paid by the Plan; and (b) legal expenses paid by NASCO for representation of its own interests or the interests of any party other than the Plan. For purposes of determining the amount of Attorney Fees the Plan may reimburse to NASCO under this exemption, the amount of reasonable attorney fees paid by NASCO on behalf of the Plan in connection with the Claims must be reduced by the amount of legal fees

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<sup>99</sup> Under the Contribution and Assignment Agreement, if the Plan receives litigation or settlement proceeds from the Claims, the proceeds would first flow to the Trust, and then each Plan's pro rata portion of the proceeds would be deposited into the individual trust funding that Plan.



received by NASCO in connection with the Claims from any non-Plan party (for example, from a third party pursuant to a court award).

13. The Plan must ultimately receive at least the full value of the promised Restorative Payments, minus the Attorney Fees. The Plan may ultimately receive more than the Restorative Payment amount required under the Contribution and Assignment Agreement. If the Plan receives litigation or settlement proceeds that exceed the amount of Restorative Payments that NASCO has made to the Plan, the Plan's Repayment to NASCO will be limited to the amount of Restorative Payments actually made by NASCO, plus Attorney Fees. For example, if NASCO has made \$22,800,000 in Restorative Payments to the Plan and reasonably incurred \$100,000 in Attorney Fees, and the Plan receives \$50,000,000 in litigation proceeds, the Plan will make a Repayment to NASCO totaling \$22,900,000.

14. Alternatively, if the Plan receives less litigation or settlement proceeds than the amount of Restorative Payments that NASCO has made to the Plan, the Plan will transfer to NASCO the lesser amount of litigation or settlement proceeds, plus Attorney Fees. For example, if NASCO has made \$22,800,000 in Restorative Payments to the Plan and has reasonably incurred \$100,000 in Attorney Fees, and the Plan receives \$10,000,000 in litigation proceeds, the Plan will not make any Repayment to NASCO.

Under this scenario, NASCO will remain obligated to complete the Restorative Payments to the Plan (totaling \$50,000,000) by December 31, 2025, prior to the Plan making any 10,100,000 Repayment to NASCO.

15. The Department notes that if the Plan receives any restitution that is tied to the conduct underlying the Claims but was ordered pursuant to a proceeding or directive that is external to Case number 20-CIV-07606, the disposition of such proceeds must conform to the requirements of this exemption.

16. NASCO retained Gallagher Fiduciary Advisors, LLC (Gallagher or the Independent Fiduciary) of New York, New York, to serve as the Plan's independent fiduciary with respect to the Required Restorative Payments and the potential repayment by the Plan of those Payments (collectively, the Proposed Transactions). Gallagher represents that it has extensive experience in institutional investment consulting and fiduciary decision-making regarding traditional and alternative investments. Gallagher further represents that its independent fiduciary decision-making work involves acting as a fiduciary advisor or decision-maker for plans and other ERISA-regulated asset pools and that it has experience with a wide range of asset classes and litigation claims.

17. Gallagher represents that it understands its duties and responsibilities under ERISA in acting as a

fiduciary on behalf of the Plan. Gallagher also acknowledges that it is authorized to take all appropriate actions to safeguard the Plan's interests, and that it will monitor the Proposed Transactions on the Plan's behalf on a continuous basis and throughout the term required by this exemption.

18. Gallagher represents that it does not have any prior relationship with any parties in interest to the Plan, including NASCO and any NASCO affiliates. Gallagher further represents the total revenues it has received from the Plan and from parties in interest to the Plan in connection with its engagement as Independent Fiduciary represents approximately 0.78% of Gallagher's total revenue.

19. Gallagher represents that no party associated with this exemption application has or will indemnify it, in whole or in part, for negligence of any kind and/or any violation of state or federal law that may be attributable to Gallagher's performance of its duties as Independent Fiduciary to the Plan with respect to the Proposed Transactions. In addition, no contract or instrument entered into by Gallagher as Independent Fiduciary may purport to waive any liability under state or federal law for any such violation.

20. On March 1, 2021, Gallagher completed an Independent Fiduciary Report (the Independent Fiduciary

Report) finding that the massive losses caused by the Trust's investment in the Allianz Structured Alpha Strategy resulted in a significant reduction to the Plan's total assets and funding level. Gallagher represents that the Required Restorative Payments, which will be received by the Plan substantially in advance of a final resolution of the Claims against Allianz and Aon, should restore the Plan's funded percentage to its pre-loss funded percentage as of January 1, 2019. The restoration of the Plan's funding status will secure ongoing benefit payments to participants and beneficiaries.

Gallagher notes that the Contribution and Assignment Agreement provides that the Trust must reimburse NASCO only up to the Required Restorative Payment Amount received by the Plan, plus any reasonable legal expense paid to non-NASCO-related parties that were incurred by, or allocated to, NASCO as a result of the Claims.<sup>100</sup> Thus, if the Plan's ultimate recovery amount from the Claims is less than the Required Restorative Payment Amount, plus related litigation expenses that were allocated to the Plan, NASCO, not the Plan, will suffer the loss.

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<sup>100</sup> Currently, legal fees and expenses associated with the Claims are being paid by most of the Participating Plan's trusts on a pro rata basis according to each Participating Plan's total invested assets held in the Master Trust's Allianz Structured Alpha Strategy before the losses were incurred in the first quarter 2020. The Applicant represents that the Committee reviews and approves these legal fees before passing them through to each Participating Plan.

Gallagher states that the Proposed Transactions and the terms of the Contribution and Assignment Agreement were negotiated and approved by Gallagher in its role as the Plan's Independent Fiduciary. Gallagher states that it approved the Proposed Transactions only after conducting an extensive analysis of the damages suffered by the Plan as a result of the failed Allianz Structured Alpha Strategy. Gallagher represents that it conducted numerous discussions with Trust representatives and counsel, along with the Plan's representatives and counsel to ensure that the interests of the Plan's participants and beneficiaries were protected with respect to all aspects of the Proposed Transactions. Based upon its assessment, Gallagher approved the Plan's receipt of the Required Restorative Payments from NASCO in exchange for the Assignment.

#### ERISA Analysis

21. Absent an exemption, the Plan's receipt of the Restorative Payments from NASCO in exchange for the Plan's transfer of litigation or settlement proceeds to NASCO would violate ERISA. In this regard, ERISA Section 406(a)(1)(A) prohibits a plan fiduciary from causing the plan to engage in a transaction if the fiduciary knows or should know that such transaction constitutes a direct or indirect sale or exchange of any property between a plan and a party in interest. NASCO, as an employer whose

employees are covered by the Plan, is a party in interest with respect to the Plan under ERISA Section 3(14)(C). The Required Restorative Payments to the Plan and the Plan's potential repayment to NASCO with litigation or settlement proceeds would constitute impermissible exchanges between the Plan and a party-in-interest (NASCO) in violation of ERISA Section 406(a)(1)(A).

ERISA Section 406(a)(1)(B) prohibits the lending of money or other extension of credit between a plan and a party-in-interest. NASCO's promise to make Required Restorative Payments to the Plan, over time, constitutes an impermissible extension of credit between the Plan and a party-in-interest in violation of ERISA Section 406(a)(1)(B).

ERISA Section 406(a)(1)(D) prohibits a plan fiduciary from causing a plan to engage in a transaction if the fiduciary knows or should know that the transaction constitutes a direct or indirect transfer to, or use by or for the benefit of, a party-in-interest, of the income or assets of the plan. The transfer of Plan assets to NASCO in connection with the Repayment would constitute an impermissible transfer of Plan assets to a party-in-interest in violation of ERISA Section 406(a)(1)(D).

#### Conditions

22. This proposed exemption contains a number of conditions that must be met. For example, the proposed

exemption mandates that the Independent Fiduciary, in full accordance with its obligations of prudence and loyalty under ERISA Section 404(a)(1)(A) and (B) must:

(a) review, negotiate, and approve the terms and conditions of the Required Restorative Payments, the Repayment, and the Contribution and Assignment Agreement, before the Plan enters into such payments and the agreement;

(b) determine that the terms and conditions of the Required Restorative Payments, the Repayment, and the Contribution and Assignment Agreement are prudent, in the interest of the Plan and its participants and beneficiaries, and protective of the rights of the Plan's participants and beneficiaries;

(c) confirm that the Required Restorative Payments are fully and timely made;

(d) monitor the Claims and confirm that the Plan receives its proper share of any litigation or settlement proceeds received by the Trust in connection with the Claims;

(e) ensure that any Repayment by the Plan to NASCO fully complies with the terms of this exemption and is for no more than the lesser of the total Restorative Payments actually made to the Plan by NASCO or the amount the Plan received from the Claims, plus Attorney Fees;

(f) ensure that any Repayment by the Plan to NASCO for legal expenses in connection with the Claims is limited to only reasonable legal expenses that were paid by NASCO to unrelated third parties for representation of the Plan and its interests (as opposed to representation of NASCO or the interests of any party other than the Plan) where NASCO was not otherwise reimbursed from a non-Plan party;

(g) monitor the Plan's Assigned Interests on an ongoing basis to determine and confirm that any excess recovery amount from the Claims (i.e., any amount that exceeds the Required Restorative Payment Amount) is retained by the Plan;

(h) ensure that all of the conditions and definitions of this proposed exemption are met; and

(i) represent that it has not and will not enter into any agreement or instrument that violates ERISA Section 410 or Department Regulations codified at 29 CFR section 2509.75-4.<sup>101</sup>

23. This proposed exemption also requires Gallagher to respond in writing to any information requests from the Department regarding Gallagher's activities as the Plan's Independent Fiduciary. Additionally, no later than 90 days after the resolution of the litigation, Gallagher must

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<sup>101</sup> ERISA Section 410 provides, in part, that "except as provided in ERISA Sections 405(b)(1) and 405(d), any provision in an agreement or instrument which purports to relieve a fiduciary from responsibility or liability for any responsibility, obligation, or duty under this part [meaning Part 4 of Title I of ERISA] shall be void as against public policy."



submit a written report to the Department demonstrating that all terms and conditions of the exemption have been met.

24. This proposed exemption requires that the Plan has not and will not release any claims, demands and/or causes of action it may have against: (a) any fiduciary of the Plan; (b) any fiduciary of the Trust; (c) NASCO; and/or (d) any person or entity related to a person or entity described in (a)-(c) of this paragraph. Additionally, any Repayment by the Plan to NASCO must be made in a manner designed to minimize unnecessary costs and disruption to the Plan and its investments.

25. The Plan may not make any Repayment to NASCO before the date: the Plan has received from NASCO the entire amount of the Restorative Payments agreed to in the Amended Contribution and Assignment Agreement; and all the Claims are settled. Furthermore, the Plan may not pay any interest to NASCO in connection with its receipt of the Required Restorative Payments, nor pledge Plan assets to secure any portion of the Required Restorative Payments.

26. Pursuant to this proposed exemption, the Plan may not incur any expenses, commissions, or transaction costs in connection with the Proposed Transactions. However, as noted above, under certain circumstances the Plan may reimburse NASCO for reasonable legal expenses arising from the Claims that NASCO paid to non-NASCO-related parties for

representation of the Plan and its interests (as opposed to representation of NASCO or the interests of any party other than the Plan) where NASCO was not otherwise reimbursed by a non-Plan party.

27. Finally, the exemptive relief provided under this proposed exemption is conditioned upon the Department's assumption that the material facts and representations set forth above in the Summary of Facts and Representation section are true and accurate at all times. In the event that a material fact or representation detailed above is untrue or inaccurate, the exemptive relief provided under this exemption will cease immediately.

#### Statutory Findings

28. ERISA Section 408(a) provides, in part, that the Department may not grant an exemption unless the Department finds that the exemption is administratively feasible, in the interest of affected plans and of their participants and beneficiaries, and protective of the rights of such participants and beneficiaries. Each of these criteria is discussed below.

a. The Proposed Exemption Is "Administratively Feasible." The Department has tentatively determined that the proposed exemption is administratively feasible because, among other things, the Independent Fiduciary will represent the interests of the Plan for all purposes with respect to

the Proposed Transactions.<sup>102</sup> In this regard, not later than 90 days after the resolution of the litigation, the Independent Fiduciary must submit a written report to the Department demonstrating that all of the requirements of this exemption have been met.

b. The Proposed Exemption Is "In the Interests of the Plan." The Department has tentatively determined that the proposed exemption is in the interest of the Plan because, among other things, the Plan's receipt of the Required Restorative Payments will substantially improve the Plan's funding status, which will enhance the Plan's ability to meet its obligations to fund benefit obligations to participants and beneficiaries and help the Plan avoid the imposition of benefit limitations imposed under Code section 436.

c. The Proposed Exemption Is "Protective of the Plan." The Department has tentatively determined that the proposed exemption is protective of the rights of the Plan's participants and beneficiaries because, among other things, the Plan will repay NASCO the lesser of the Required Restorative Payment Amount received by the Plan, or the

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<sup>102</sup> This proposed exemption would require that if the Independent Fiduciary resigns, is removed, or for any reason is unable to serve as an Independent Fiduciary, the successor Independent Fiduciary must, among other things, assume all of the duties of the outgoing Independent Fiduciary. As soon as possible, including before the appointment of a successor Independent Fiduciary, the Plan Sponsor and the Plan must notify the Department's Office of Exemption Determinations of the change in Independent Fiduciaries. The notification must contain all material information including the qualifications of the successor Independent Fiduciary.

amount the Plan receives in proceeds from the Claims, ensuring that the Proposed Transactions will result in an increase in Plan assets of at least the total amount of Restorative Payments (less reasonable legal expenses related to the Claims paid by NASCO to unrelated third parties, as confirmed and approved by the Independent Fiduciary). Further, this exemption preserves any right, claim, demand and/or cause of action the Plan may have against: (a) any fiduciary of the Plan; (b) any fiduciary of the Trust; (c) NASCO; and/or (d) any person or entity related to a person or entity described in (a)-(c).

#### Summary

29. Based on the conditions described above, the Department has tentatively determined that the relief sought by the Applicant satisfies the statutory requirements under ERISA Section 408(a) for the Department to make findings that support its issuance of a proposed exemption.

#### **PROPOSED EXEMPTION**

The Department is considering granting an exemption under the authority of ERISA Section 408(a) and Code Section 4975(c)(2) and in accordance with the procedures

set forth in the Department's exemption procedure regulation.<sup>103</sup>

## **Section I. Definitions**

(a) The term "Attorney Fees" means reasonable legal expenses paid by NASCO on behalf of the Plan in connection with the Claims, if such fees are reviewed and approved by a qualified independent fiduciary who confirms that the fees were reasonably incurred and paid by NASCO to unrelated third parties. For the purposes of this exemption, the Attorney Fees reimbursable to NASCO do not include: (1) legal expenses paid by the Plan; and (2) legal expenses paid by NASCO for representation of NASCO or the interests of any party other than the Plan.

(b) The term "NASCO" means National Account Service Company LLC.

(c) The term "Claims" means the legal claims against Allianz Global Investors U.S. LLC (Allianz) and Aon Investments USA Inc. (Aon), to recover certain losses incurred by the Plan in the first quarter of 2020.

(d) The term "Contribution and Assignment Agreement" means the written agreement between NASCO and the Plan, dated March 1, 2021, containing all material terms regarding NASCO's agreement to make Required Restorative Payments to the Plan in return for the Plan's potential

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<sup>103</sup> 29 CFR part 2570, subpart B (55 FR 32836, 32847, August 10, 1990).

Repayment to NASCO of an amount that is no more than lesser of the Required Restorative Payment Amount (as described in Section I(h)) received by the Plan or the amount of litigation proceeds the Plan receives from the Claims, plus reasonable attorney fees paid to unrelated third parties by NASCO in connection with the Claims.

(e) The term "Independent Fiduciary" means Gallagher Fiduciary Advisors, LLC (Gallagher) or a successor Independent Fiduciary to the extent Gallagher or the successor Independent Fiduciary continues to serve in such capacity who:

(1) Is not an affiliate of NASCO and does not hold an ownership interest in NASCO or affiliates of NASCO;

(2) Was not a fiduciary with respect to the Plan before its appointment to serve as the Independent Fiduciary;

(3) Has acknowledged in writing that it:

(i) is a fiduciary with respect to the Plan and has agreed not to participate in any decision regarding any transaction in which it has an interest that might affect its best judgment as a fiduciary; and

(ii) Has appropriate technical training or experience to perform the services contemplated by the exemption;

(4) Has not entered into any agreement or instrument that violates the prohibitions on exculpatory

provisions in ERISA Section 410 or the Department's regulation relating to indemnification of fiduciaries;<sup>104</sup>

(5) Has not received gross income from NASCO or its affiliates during any fiscal year in an amount that exceeds two percent (2%) of the Independent Fiduciary's gross income from all sources for the prior fiscal year. This provision also applies to a partnership or corporation of which the Independent Fiduciary is an officer, director, or 10 percent (10%) or more partner or shareholder, and includes as gross income amounts received as compensation for services provided as an independent fiduciary under any prohibited transaction exemption granted by the Department; and

(6) No organization or individual that is an Independent Fiduciary, and no partnership or corporation of which such organization or individual is an officer, director, or ten percent (10%) or more partner or shareholder, may acquire any property from, sell any property to, or borrow any funds from NASCO or from affiliates of NASCO while serving as an Independent Fiduciary. This prohibition will continue for six months after the party ceases to be an Independent Fiduciary and/or the Independent Fiduciary negotiates any transaction on behalf of the Plan during the period that the

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<sup>104</sup> 29 CFR 2509.75-4.

organization or individual serves as an Independent Fiduciary.

(f) The "Plan" means the Non-Contributory Retirement Program for Certain Employees of National Account Service Company.

(g) The term "Plan Losses" means the \$51,662,561 in Plan losses the BCBSA's National Employee Benefits Committee alleges were the result of breaches of fiduciary responsibilities and breaches of contract by Allianz Global Investors U.S. LLC and/or Aon Investments USA Inc.

(h) The term "Restorative Payments" means the \$50 Million in payments NASCO is required to pay the Plan by December 21, 2025, as set forth in the Contribution and Assignment Agreement.

(i) The "Repayment" means the payment, if any, that the Plan will transfer to NASCO following the Plan's receipt of proceeds from the Claims, where the Repayment is made following the full and complete resolution of the Claims, and in a manner that is consistent with the terms of the exemption.

## **Section II. Proposed Transactions**

If the proposed exemption is granted, the restrictions of ERISA Sections 406(a)(1)(A), (B) and (D) and the sanctions resulting from the application of Code Section 4975, by reason of Code Sections 4975(c)(1)(A), (B) and



(D), shall not apply, effective September 2, 2020, to the following transactions: NASCO's transfer of Restorative Payments to the Plan; and, in return, the Plan's Repayment of an amount to NASCO, which must be no more than the lesser of the Restorative Payment received by the Plan or the amount of litigation proceeds the Plan received from the Claims, plus reasonable Attorney Fees, provided that the Definitions set forth in Section I and the Conditions set forth in Section III are met.

**Section III. Conditions**

(a) The Plan receives the entire Restorative Payment Amount no later than December 31, 2025;

(b) In connection with its receipt of the Required Restorative Payments, the Plan does not release any claims, demands and/or causes of action the Plan may have against the following: (1) any fiduciary of the Plan; (2) any fiduciary of the Trust; (3) NASCO; and/or (4) any person or entity related to a person or entity identified in (1)-(3) of this paragraph;

(c) The Plan's Repayment to NASCO is for no more than the lesser of the total Restorative Payments received by the Plan or the amount of litigation proceeds the Plan receives from the Claims. The Plan's Repayment to NASCO may only occur after the Independent Fiduciary has determined that: all the conditions of the exemption are

met; the Plan has received all the Restorative Payments it is due; and the Plan has received all the litigation proceeds it is due. The Plan's Repayment to NASCO must be carried out in a manner designed to minimize unnecessary costs and disruption to the Plan and its investments;

(d) A qualified independent fiduciary (the Independent Fiduciary, as further defined in Section II(e)), acting solely on behalf of the Plan in full accordance with its obligations of prudence and loyalty under ERISA Sections 404(a)(1)(A) and (B) must:

(1) Review, negotiate and approve the terms and conditions of the Restorative Payments and the Repayment and the Contribution and Assignment Agreement, all of which must be in writing, before the Plan enters into those transactions/agreement;

(2) Determine that the Restorative Payments, the Repayment, and the terms of the Contribution and Assignment Agreement, are prudent and in the interest of the Plan and its participants and beneficiaries;

(3) Confirm that the Required Restorative Payment Amount was fully and timely made;

(4) Monitor the litigation related to the Claims and confirm that the Plan receives, in a timely manner, its proper share of any litigation or settlement proceeds received by the Trust;

(5) Ensure that any Repayment by the Plan to NASCO for legal expenses in connection with the Claims is limited to only reasonable legal expenses that were paid by NASCO to unrelated third parties;

(6) Ensure that all of the conditions and definitions of this proposed exemption are met;

(7) Submit a written report to the Department's Office of Exemption Determinations demonstrating and confirming that the terms and conditions of the exemption were met, within 90 days after the Repayment; and

(8) Not enter into any agreement or instrument that violates ERISA Section 410 or the Department's Regulations codified at 29 CFR Section 2509.75-4.

(f) The Plan pays no interest in connection with the Restorative Payments;

(g) The Plan does not pledge any Plan assets to secure any portion of the Restorative Payments;

(h) The Plan does not incur any expenses, commissions, or transaction costs in connection with the Proposed Transactions. However, if first approved by the Independent Fiduciary, the Plan may reimburse NASCO for reasonable legal expenses paid in connection with the Claims by NASCO to non-NASCO-related parties. For purposes of determining the amount of Attorney Fees the Plan may reimburse to NASCO under this proposal, the amount of reasonable attorney fees paid by NASCO on behalf of the

Plan in connection with the Claims must be reduced by the amount of legal fees received by NASCO in connection with the Claims from any non-Plan party (i.e., pursuant to a court award);

(i) The proposed transactions do not involve any risk of loss to either the Plan or the Plan's participants and beneficiaries;

(j) No party associated with this exemption has or will indemnify the Independent Fiduciary and the Independent Fiduciary will not request indemnification from any party, in whole or in part, for negligence and/or any violation of state or federal law that may be attributable to the Independent Fiduciary in performing its duties to the Plan with respect to the Proposed Transactions. In addition, no contract or instrument may purport to waive any liability under state or federal law for any such violation.

(k) If an Independent Fiduciary resigns, is removed, or for any reason is unable to serve as an Independent Fiduciary, the Independent Fiduciary must be replaced by a successor entity that: (1) meets the definition of Independent Fiduciary detailed above in Section II(e); and (2) otherwise meets all of the qualification, independence, prudence and diligence requirements set forth in this exemption. Further, any such successor Independent Fiduciary must assume all of the duties of the outgoing

Independent Fiduciary. As soon as possible, including before the appointment of a successor Independent Fiduciary, NASCO must notify the Department's Office of Exemption Determinations of the change in Independent Fiduciary and such notification must contain all material information regarding the successor Independent Fiduciary, including the successor Independent Fiduciary's qualifications; and

(1) All of the material facts and representations set forth in the Summary of Facts and Representation are true and accurate at all times.

#### NOTICE TO INTERESTED PERSONS

The Applicant will give notice of the proposed exemption to all interested persons and all of the parties to the litigation described above, within fifteen calendar days after the publication of the notice of proposed exemption in the *Federal Register*. The notice will contain a copy of the notice of proposed exemption, as published in the *Federal Register*, and a supplemental statement, as required pursuant to the Department's regulations codified at 29 CFR 2570.43(a)(2). The supplemental statement will inform interested persons of their right to comment on the pending exemption. Written comments are due by [INSERT DATE THAT IS 45 DAYS FROM THE PUBLICATION OF THE NOTICE IN THE *FEDERAL REGISTER*].

All comments will be made available to the public.

**Warning:** If you submit a comment, EBSA recommends that you include your name and other contact information in the body of your comment, but DO NOT submit information that you consider to be confidential, or otherwise protected (such as a Social Security number or an unlisted phone number) or confidential business information that you do not want publicly disclosed. All comments may be posted on the Internet and can be retrieved by most Internet search engines.

*For Further Information Contact:* Mr. Joseph Brennan of the Department, telephone (202) 693-8456. (This is not a toll-free number.)

#### **GENERAL INFORMATION**

The attention of interested persons is directed to the following:

(1) The fact that a transaction is the subject of an exemption under section 408(a) of the Act and/or section 4975(c)(2) of the Code does not relieve a fiduciary or other party in interest or disqualified person from certain other provisions of the Act and/or the Code, including any prohibited transaction provisions to which the exemption does not apply and the general fiduciary responsibility

provisions of section 404 of the Act, which, among other things, require a fiduciary to discharge his duties respecting the plan solely in the interest of the participants and beneficiaries of the plan and in a prudent fashion in accordance with section 404(a)(1)(B) of the Act; nor does it affect the requirement of section 401(a) of the Code that the plan must operate for the exclusive benefit of the employees of the employer maintaining the plan and their beneficiaries;

(2) Before an exemption may be granted under section 408(a) of the Act and/or section 4975(c)(2) of the Code, the Department must find that the exemption is administratively feasible, in the interests of the plan and of its participants and beneficiaries, and protective of the rights of participants and beneficiaries of the plan;

(3) The proposed exemptions, if granted, will be supplemental to, and not in derogation of, any other provisions of the Act and/or the Code, including statutory or administrative exemptions and transitional rules. Furthermore, the fact that a transaction is subject to an administrative or statutory exemption is not dispositive of whether the transaction is in fact a prohibited transaction; and

(4) The proposed exemptions, if granted, will be subject to the express condition that the material facts and representations contained in each application are true

and complete, and that each application accurately describes all material terms of the transaction which is the subject of the exemption.

Signed at Washington, DC, this 16th day of August, 2022.

**Timothy D. Hauser,**

*Deputy Assistant Secretary for Program Operations,  
Employee Benefits Security Administration,  
U.S. Department of Labor.*

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